

**Before the
Federal Communications Commission
Washington, D.C. 20554**

In the Matter of)	
)	
Developing a Unified Intercarrier)	CC Docket No. 01-92
Compensation Regime)	
)	

FURTHER NOTICE OF PROPOSED RULEMAKING

**Comments
of
THE RURAL ALLIANCE**

May 23, 2005

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I. EXECUTIVE SUMMARY

The Rural Alliance respectfully submits these Comments in the above-captioned proceeding. The Rural Alliance was initially formed by the Alliance for Rational Inter-carrier Compensation (“ARIC”) and the Expanded Portland Group (“EPG”) in order to unite their respective efforts to promote inter-carrier compensation and universal service solutions that will meet the needs of the changing telecommunications marketplace while providing rural consumers with affordable access to basic and advanced telecommunications services. Prior to the unification of their respective efforts, ARIC and EPG each filed proposals for consideration in this proceeding which are among those with respect to which the Federal Communications Commission (“Commission”) has specifically sought comment in this Further Notice of Proposed Rulemaking (“*FNPRM*”).

A large and growing number of rural telephone company service providers and associations have joined together with ARIC and EPG in the efforts of the Rural Alliance.¹ Together, these companies and organizations have unified their efforts to review both the proposals of other parties submitted in this proceeding and the extensive issues raised by the *FNPRM*. The initial results of this unified effort are presented in these Comments and include:

1. A framework of guiding principles to which revisions in inter-carrier compensation and universal service mechanisms must adhere in order to address the changes that are occurring in the telecommunications industry and to advance the nation’s fundamental universal service goals;

¹ The membership in the Rural Alliance currently consists of more than 200 individual rural telephone companies, as well as associations representing several hundred companies. The current membership in the Rural Alliance is set forth in Appendix A. The Rural Alliance respectfully reserves the right to supplement this list as membership in the Alliance continues to grow during the course of this proceeding.

2. An evaluation of other parties' proposals for changes in intercarrier compensation, which will not reasonably address the changes occurring in the telecommunications market and are inconsistent with the fundamental principles necessary to preserve and foster universal service and advanced services in rural areas;
3. An analysis of the need to ensure that a collaborative effort between federal and state regulators addresses modifications in intercarrier compensation associated with removing the existing distinctions in interconnection rates based on jurisdiction;
4. A response to each of the issues set forth in the *FNPRM*: legal, network interconnection, cost recovery, implementation, so-called "transit service," and Commercial Mobile Ratio Service ("CMRS"). These responses are offered specifically from the perspective of rural customers and their carriers and the impact of the resolution of these issues on the provision of universal and advanced services in rural areas;
5. An analysis of the need for thorough consideration of traffic bound for Internet Service Providers ("ISP") and Internet Protocol ("IP") interconnection, together with the associated evolving intercarrier compensation requirements; and
6. An analysis of the real costs and resulting detriment of proposals to implement "bill and keep."

The Commission, in this *FNPRM*, is seeking comment on the intercarrier compensation structure that applies during the transition from a circuit-switched environment to a packet-switched environment. This proceeding is neither the first time that the Commission and the telecommunications industry have addressed the need to revise intercarrier compensation, nor is this the first instance where technological change has served as the catalyst for needed reform. Moreover, this proceeding is not the first, and undoubtedly will not be the last, where parties attempt to utilize the proceeding as a forum to obtain short-term business objectives.

While technological evolution is a driving force behind the need for reforms, several underlying principles that have served as the foundation for intercarrier compensation and resulting rate design and cost recovery mechanisms that have fostered the provision of universal service still make sense in this changing environment. While numerous parties may promote the implementation of “bill and keep” as a wholesale replacement for the existing intercarrier compensation framework, bill and keep ignores not only existing law and regulation, but also sound public policy.²

Subsequent to a review of the comments filed by other parties, the Rural Alliance intends to provide Reply Comments and to offer responsive refinements incorporating aspects of the ARIC and EPG plans and other parties’ proposals that are consistent with the Rural Alliance’s guiding principles.

A. The Rural Alliance Embraces Appropriate Changes to Intercarrier Compensation.

Technology is changing and will forever alter how service is provided to customers. Although rural carriers face unique challenges, rural carriers are making changes to their networks, just as urban carriers are. The principles established by the Rural Alliance embrace the changes that are upon the industry, and, in fact, the plans that have been submitted in the record by ARIC and EPG not only discuss the transition but are the only plans that propose specific consideration for an all-IP environment.

Rural Alliance members embrace these changes because the technology provides new opportunities for rural economic development and new services and features to

² The issues and matters addressed throughout this Executive Summary are thoroughly set forth in the body of these Comments and the Appendix. For example, the concerns with bill-and-keep proposals are

improve the lives of rural consumers. The new opportunities created by emerging services will not happen without a modern, broadband-capable network. The Rural Alliance envisions that an underlying network, albeit packet switched, will be utilized to deliver services that cannot even be conceived of today. Sustaining revenue streams to rural carriers is necessary to support the existing and future infrastructure.

Prices that are not set to accurately reflect the cost of producing a good or service, will not achieve economic efficiency. Rather than requiring only end-users who order a connection to pay for the network, the Rural Alliance believes that requiring payment for network usage from all network users, including other carriers, will promote economic efficiency, as demand for the network will be based on the cost of using the network. Because bill and keep is not cost based, it will create new incentives for arbitrage and will result in unintended consequences, such as costly switching and transport resources being consumed without the owner of those facilities being compensated. Finally, the adoption of the “edge” network interconnection proposal in the Intercarrier Compensation Forum (“ICF”) plan would require rural carriers to carry traffic for long distances without adequate compensation.

Bill and keep is a unified compensation scheme with a rate of zero. The efficiencies associated with *voluntary* bill and keep do not apply to *mandatory* bill and keep arrangements. Bill and keep generally will not be efficient, except in those circumstances with balanced traffic and cost structures. For services that are not reciprocal in nature, such as the origination or termination of traffic for retail interexchange carriers (“IXCs”), bill and keep is neither efficient nor fair to the wholesale

addressed in detail in these Comments, *infra*, and in the white paper set forth in the Appendix B hereto.

service provider — the Local Exchange Carrier (“LEC”). Because IXC’s still provide end-to-end, retail long distance and 800 service, the elimination of originating charges for exchange access is illogical. These originating service obligations cause cost for the LEC, but provide no value to the LEC’s operations in the absence of originating access charges. Other industries where inter-firm compensation takes place in an unregulated setting do *not* generally use bill and keep.³

The Commission must establish a compensation mechanism that recognizes the changes in technology and the market, emphasizes sound economic principles, complies with existing law, promotes efficient use of the network, minimizes or eliminates arbitrage opportunities, and preserves and advances universal service. The Rural Alliance principles balance all of these factors. The Rural Alliance supports payment of a uniform, cost-based intercarrier compensation rate by entities that use the underlying network, a local rate benchmark, a reasonable transition period, a new mechanism or changes to existing universal service to provide for recovery of reductions in intercarrier compensation, and cooperative and collaborative processes between the Commission and the States to address these issues.

B. Technology and Market Changes Require Continual Reassessment of Intercarrier Compensation.

The concept that more than a single carrier is often involved in the provision of end-to-end telecommunications services is hardly new to the Commission or the telecommunications industry. Long before the passage of the Telecommunications Act of 1996, the Communications Act of 1934 (the “Act”) incorporated recognition of this

³ Such industries include Internet backbone service, wireless roaming and financial interchange fees.

concept and the fundamental need for intercarrier compensation into section 201 of the Act:

(a) It shall be the duty of every common carrier engaged in interstate or foreign communication by wire or radio to furnish such communication service upon reasonable request therefor; and, in accordance with the orders of the Commission, in cases where the Commission, after opportunity for hearing, finds such action necessary or desirable in the public interest, to establish physical connections with other carriers, *to establish through routes and charges applicable thereto and the divisions of such charges, and to establish and provide facilities and regulations for operating such through routes.*⁴

The italicized provision of section 201(a) cited above is the very foundation of both the source and the requirement for intercarrier compensation. More than the facilities of a single carrier are involved in the provision of end-to-end service. The customer pays a single rate to one of the service providers and the service provider, in turn, compensates the carriers that own the underlying network or networks that are used to provide the service.

Fundamental to the establishment of rational rate design structures for intercarrier compensation is the concept of jurisdictional cost allocation of joint and common costs. While the jurisdictional cost allocation rules (set forth, respectively, in Parts 36 and 69 of the Commission's Rules) appear complicated, the fundamental concepts are easily understood. The plant, and associated expenses, generally required for the provision of basic telephone service is utilized by customers to make and receive local calls, intrastate toll calls, interstate toll calls, and international calls, and to connect to the Internet.

⁴ 47 U.S.C. section 201(a), emphasis added.

While the establishment of connectivity to the nationwide switched telephone network and to the Internet is of benefit to the customer that orders the connectivity, a fundamental principle of ratemaking relies on the concept that all others who can use the same plant to call and be called by the customer also benefit. This principle provides the foundation of the existing and prior intercarrier compensation structures that have inherently and purposefully recognized the need for rate design structures that will foster the provision of universal and advanced services in rural areas.

The fundamental concept of jurisdictional cost allocation has been the lynchpin that has ensured that the joint and common costs necessary to operate the entire network of a LEC are reasonably allocated on a jurisdictional basis, and that rates are established for each jurisdictional service to recover the apportioned costs.⁵ Pursuant to section 410(c) of the Act, matters concerning jurisdictional allocations of LEC property and expenses are referred to a Federal-State Joint Board. State and Commission members of the Joint Boards have traditionally worked together to determine joint cost allocations in a manner that has preserved and promoted universal service. Regulators have recognized and applied the clear distinction in the utilization of telephone plant in urban and rural areas in their jurisdictional allocation and rate design decisions.⁶

Prior to divestiture of the Bell System in 1984, each LEC recovered its allocated interstate costs through an interstate toll division of revenue process with the connecting Bell System carrier. The Commission and State regulators recognized that rational

⁵ Smith v. Illinois Bell, 282 U.S. 133 (1930).

⁶ Within urban areas (*e.g.*, “inside and around the beltway” of Washington, D.C.), a customer is often able to call and be called by hundreds of thousands (and often millions) of other customers on a toll-free basis. In less populated rural areas, however, customers can most often reach and be reached by only a few thousand (and sometimes only a few hundred) other customers on a toll-free basis.

jurisdictional cost allocation rules required consideration of the geographic and demographic characteristics of the areas served by rural carriers. The allocated interstate costs of the Rural Local Exchange Carrier (“RLEC”) networks were, in turn, incorporated in the expenses associated with the establishment of interstate toll rates. Accordingly, the interstate costs were ultimately spread across all interstate toll users, who had the luxury of being able to call to, or to receive a call from, the rural subscriber.

The divestiture of the Bell System and the implementation of interstate toll competition ended the interstate division of settlements process and established interstate access charges as its replacement. Instead of recovering interstate allocated costs through a contractual settlements process, RLECs recovered interstate costs through the access charges that IXC pay to receive and terminate calls through the RLEC network. IXCs, in turn, recover their access charge expenses through the rates charged end users for long-distance calls. Accordingly, the intercarrier compensation expenses borne by the IXCs were still ultimately spread among all toll users, who continued to have the luxury of being able to call to, or to receive a call from, rural subscribers.

When the access charge rules were established, customers depended primarily on IXC toll service to reach customers in other localities. The more-recent rapid migration to wireless services and Internet-based service to reach and be reached by other customers was not contemplated. The Rural Alliance joins with other parties that urge the need for change in the framework of intercarrier compensation to reflect the evolution in both technology and the marketplace.

The Rural Alliance takes exception to those parties that urge “quick-fix” bill-and-keep proposals that overlook the underlying foundation of the principles originally

incorporated into the “division of revenues” process and later retained in the current access charge rate design structure. Consistent with applicable law, Federal and State regulators have established reasonable measures to apportion joint and common plant and expenses on a jurisdictional basis that reflected both usage and value of the network for rural subscribers.

No rational basis exists to depart from this fundamental framework that continues to be supported by existing law, regulation and public policy. The Rural Alliance accordingly urges meaningful consideration of proposals, such as those set forth by ARIC and EPG, which apply these principles to the evolving technology and marketplace. The Rural Alliance is concerned that the proposals of some other parties advocating preemption of State jurisdiction over intrastate interconnection overlook this fundamental framework. As the Commission is aware, joint and common costs are not categorized as interstate or intrastate until the application of the jurisdictional allocation process prescribed in the Commission’s Part 36 Rules, as adopted pursuant to Federal-State Joint Board consideration.⁷ Not only should the Commission consider the historical fundamental framework, existing law, regulation and public policy, but the Commission should also consider how other competitive markets work, as well as sound economic policy.

The Commission has recognized both prior and subsequent to the passage of the 1996 Act that there is a difficult balance that must be maintained in steering a new course in regulation to promote competition and concurrently maintain and foster universal service objectives. In steering that course, the Commission has appropriately recognized

⁷ A complete discussion of these concerns is set forth in Section V, *infra*.

in other proceedings that the need for consideration of changes in both the existing access charge and universal service rules presented “interrelated issues without a single, precise solution.”⁸

Accordingly, the Commission has also recognized the need for separate review of the issues and circumstances specific to rural telephone companies and rate-of-return carriers. The agendas of other parties to this proceeding, however, appear to be driven toward a predetermined outcome — the total elimination of rural carrier access charges and intercarrier compensation. That single objective, however, is not achievable on a sustainable and rational basis when the specific characteristics and needs of rural consumers and rural carriers are considered. The Rural Alliance thus urges the Commission to ensure that the results of this proceeding are consistent with the statutory and policy goals of securing reasonably comparable prices for consumers, providing higher quality services, and encouraging the rapid deployment of new telecommunications technologies.

C. The Rural Alliance’s Principles Provide a Reasonable Basis for Intercarrier Compensation Reform.

The Commission has previously considered changes in access charge structure and universal service support mechanisms with an understanding of the need for policies reflecting the operational and market distinctions that exist between rural and non-rural

⁸ *Second Report and Order and Further Notice of Proposed Rulemaking in CC Docket No. 00-256, Fifteenth Report and Order in CC Docket No. 96-45, and Report and Order in CC Docket Nos. 98-77 and 98-166 (“MAG Order”)* at ¶ 5 citing the *Interstate Access Support Order*, 15 FCC Rcd 12962, 12978 at ¶ 38) (2000).

companies.⁹ In the past, these distinctions were not only recognized, but became the basis for Commission policy affecting rural customers and their rural incumbent providers.¹⁰ These prior Commission decisions regarding both interstate cost allocations and the appropriate rate design for cost recovery have served the nation's universal service objectives well.¹¹

The Rural Alliance Comments are organized around fundamental principles rooted in law, regulation and public policy that Federal and State regulators have utilized in promoting universal service and deploying advanced technology in rural and high-cost areas. These Comments recommend intercarrier compensation reforms that encourage long-term investment in rural telecommunications infrastructure, recognizing that ongoing investment is essential to ensuring rural markets' continued access to basic and advanced services comparable to those of urban markets.

⁹ Rural companies "generally have higher operating and equipment costs than price cap carriers due to lower subscriber density, smaller exchanges, and limited economies of scale." *See, e.g., MAG Order* at ¶ 4. The Courts have also acknowledged the rural/non-rural telephone company distinction that exists as a result of both operational and market facts, and is codified in the 1996 Act (§§ 214(e), 251, and 254). *See, e.g., Alenco Communications, Inc. v. FCC*, 201 F.3d 608 (5th Cir. 2000) ("*Alenco*") and *Qwest Corp. v. FCC*, 258 F.3d 1191 (10th Cir. 2001) ("*Qwest*").

¹⁰ *See, e.g. In the Matter of Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, *Multi-Association Group Plan for Regulation on Interstate Services of Non-Price Cap Incumbent Local Exchange Carriers and Interexchange Carriers*, CC Docket No. 00-256, Fourteenth Report and Order in CC Docket No. 96-45, and Report and Order in CC Docket No. 00-256, FCC 01-157 ("*RTF Order*") (rel. May 23, 2001).

¹¹ In fact, the Commission has previously expressed its intent to follow three specific basic policies regarding RLECs and their subscribers:

1. A rural rate-of-return regulated LEC should be permitted to establish rates for its interstate access services that recover its costs. (*See MAG Order* at ¶¶ 12, 84 and 206.)
2. Customers should not pay rates that unreasonably support services provided to other customers. (*See MAG Order* at ¶¶ 18, 23, and 43.)
3. Rates that reflect an individual carrier's cost of service provide the proper signals to permit a potential entrant to decide whether to enter a particular market. (*See MAG Order* at ¶ 84.)

As discussed in Section III, *infra*, however, the *MAG Order* disregarded the rural market characteristics that provided the basis for past practices and policies. Petitions for Reconsideration of that Order remain pending.

Appropriate intercarrier compensation pricing, based on cost, will provide the correct incentive for efficient and effective network use without overburdening the support required from universal service mechanisms. Cost-based intercarrier pricing will result in rural end-user rates that are reasonably comparable to those in urban areas, and correct intercarrier pricing acknowledges the underlying public policy that the value of the rural networks does not accrue solely to rural end-user customers. *All* customers benefit through ubiquitous connectivity.

The Rural Alliance respectfully submits that the principles set forth below provide a reasonable framework for reforming intercarrier compensation, will send the right economic signals for network use, and are essential to fulfill the Act's universal service principles and goals:

1. *Intercarrier Compensation Rates Should Be Uniform and Cost-Based.*

Unified cost-based rates should be established so that equivalent network functionality is charged at equivalent rates no matter if the traffic is terminating or originating, reciprocal compensation or access, interstate or intrastate. For rate-of-return carriers, uniform rates should be based on each carrier's embedded cost. Rate pooling and rate banding should continue to be an option.

The Commission should establish a proceeding to evaluate capacity-based intercarrier compensation charges for switched services and session-based charges for the Digital Subscriber Line rate structure.

2. *Existing Interconnection Rules Should Be Clarified Consistent with Statute.*

LECs and other carriers should continue to interconnect at existing meet points or as otherwise agreed to by the carriers. Interconnection must occur within the network area of an RLEC. Costs associated with indirect interconnection at another carrier's point of interconnection should never be borne by the RLEC. A complex, new set of interconnection rules is unnecessary and could be harmful. Rather, the application of the Commission's existing rules should be clarified consistent with the Act's intent.

3. *Retail Service Providers Should Pay for Their Network Usage.*

When a carrier's network facilities are used by a Retail Service Provider ("RSP") to provide a service to its customers, the RSP must provide appropriate compensation to the network carrier for that use. This compensation obligation exists regardless of the technology or protocol used to carry the call.

The distinction between access charges and reciprocal compensation must be retained, even though rates are unified. Originating and terminating exchange access applies when an RSP does not have a physical connection to its customers and seeks to provide an end-to-end interexchange service. Terminating reciprocal compensation, under section 251(b)(5), applies when the call is local to both carriers and the originating carrier, the RSP in this case, seeks to provide its customers with connectivity to a customer on the other carrier's network in the local area.

No LEC should be required to terminate calls if the call records do not permit billing of such traffic. A process should be developed requiring all calls to be properly labeled, and providing real-time resolution of disputes.

4. *Transiting Services Should Be Cost-Based and Available under Just and Reasonable Conditions.*

Large tandem and transit network providers currently have significant market power and are only seeking to further consolidate that power.¹² Transiting services must remain available at cost-based rates under just and reasonable conditions.

5. *Local Benchmark Rates Should Be Imputed in Revenue Replacement Funds.*

To ensure equity in the distribution of revenue replacement funds, composite local rate benchmarks, including both basic local and Subscriber Line Charge ("SLC") rates, should be imputed into the revenue replacement fund amount. The composite local benchmark should be established based upon the nationwide average urban rate level plus the current SLC cap rates. Carriers with basic local rates below the nationwide average urban level should be allowed to increase their rates in an expeditious manner without the need for State rate proceedings. Carriers with basic local rates above the nationwide average urban level should be allowed to lower those rates and draw replacement funding for the difference.

¹² This concern is likely to be exacerbated by the announced proposed mergers of SBC with AT&T and of Verizon with MCI.

6. *Revenue Replacement Payments Should Be Based on Net Revenue Losses.*

Existing Federal universal service mechanisms should be retained. Additional revenue replacement distributions should be made available to qualifying carriers based on net revenue losses as a result of the unification of intercarrier compensation rate levels, offset by local rate changes made to reach benchmark levels.

7. *Universal Service Collections Should Be Derived from the Broadest Possible Contributor Base.*

The provision of universal service throughout the nation would not be possible without universal service funding. The Federal universal service policy equally benefits all telecommunications users who can reach and be reached by those consumers located in rural and high-cost service areas. Accordingly, contributions to the new universal service collection mechanism should be derived from the broadest possible contributor base. All service providers and their customers benefit from ubiquitous and affordable network connections, and should be required to contribute to the universal service fund. Further analysis should be completed to assess how contributions should be structured, including connections and numbers-based approaches.

8. *Infrastructure-based Universal Service and IP Interconnection Oversight Are Necessary.*

Affordable and open access to IP backbone networks is essential to ensure that consumers in rural, insular and high-cost areas enjoy access to advanced services reasonably comparable to that available in urban areas. Rural carriers lack market power and should be able to interconnect with IP backbone providers under reasonable and non-discriminatory terms and conditions. Interconnection agreements should be publicly available.

Universal service funding should be targeted to provide incentives for rural infrastructure investment that will expand broadband connectivity to areas where it would not otherwise be economically viable. In the long term, separate funds should be established for broadband connectivity and mobility.

The Rural Alliance principles, as set forth above, are based on the laws, regulations and public policies that historically have been effective in directing the intercarrier compensation framework to foster and protect universal service. The

evolution of technology and the marketplace has not altered the relevance of these principles. The Rural Alliance respectfully submits that any changes to the intercarrier compensation framework must adhere to these principles.

D. The ARIC and EPG Proposals Are Consistent with the Rural Alliance Principles.

Both the ARIC plan and the EPG plan are responsive to the Rural Alliance principles enumerated above, and provide a rational framework for achieving public policy goals.

- The ARIC and EPG plans call for a unified intercarrier rate to solve the arbitrage problems that exist today. Both plans are based upon the principle that costs should be borne by cost causers, including RSPs who benefit from the availability of facilities constructed and maintained by network carriers.
- Neither plan proposes network reconfigurations or interconnection rule changes. Instead, current interconnection points within the RLEC networks are maintained.
- The cooperation of State and Federal regulators is necessary to institute intercarrier rate reform, as well as revenue replacement through a combination of local rate rebalancing and revenue replacement mechanisms.
- The ARIC and EPG proposals also maintain that pooling should remain an available option.
- Both ARIC and EPG agree that maintenance of open networks requires that market power should not interfere with the availability of transit and transport services at cost-based rates and under just and reasonable conditions.
- Each group recognizes oversight of IP interconnection is vital to ensure that rural consumers continue to have affordable Internet access.

- Finally, ARIC and EPG recognize that the universal service mechanism requires fundamental reform to sustain its viability as markets change and applications migrate to IP.

E. Other Parties' Proposals are Contrary to Existing Law, Policy and the Public Interest.

The Rural Alliance has analyzed each of the other major intercarrier compensation proposals currently before the Commission in the context of the principles described above. This inspection, detailed in the body of these Comments, reveals that each plan fails, to varying degrees, to further the critical public policy goals embodied by the Rural Alliance principles. These fundamental inadequacies, highlighted below, preclude the wholesale adoption of any of these plans.

Among the most-serious deficiencies of any plan is the movement toward adoption of mandatory bill and keep. Such an approach would violate both the principle of cost-based intercarrier compensation and the principle that RSPs must pay for network usage. The benefits of rate unification are obtainable without the distorted economic signals resulting from a mandatory bill-and-keep regime applied indiscriminately without consideration of appropriate cost levels or traffic balance. When network costs are artificially precluded from being reflected in wholesale pricing, uneconomic consumption of costly network resources will result. Increased consumption creates even greater pressure on network resources, but distorts the economic incentive of carriers to meet the demand.

When the principle of network usage payment is ignored, RSPs unfairly burden network providers. Under a bill-and-keep methodology, which embraces this deficiency,

there is no incentive to own, maintain or improve local networks. Instead, carriers are perversely encouraged to shift costs to their local facilities-based competitors. IXC without local facilities will gain an unfair advantage over other facilities-based competitors because IXCs will no longer be required to pay for network use. Any approach that fails to require payment for network usage will result in network owners being unfairly disadvantaged, and will discourage investment in such networks.

Plans promoting mandatory bill and keep ignore cost-based pricing principles and network payment principles. These plans will consequently create economic inefficiency, pricing distortions, and fundamental competitive inequities.¹³ The ICF plan further breaches cost-based intercarrier compensation and network payment principles by setting rural compensation at an insufficient level and by completely eliminating originating access.¹⁴ The ICF plan's failure to recognize the reality of rural transport distances further violates the principle of cost-based compensation rates.¹⁵ Western Wireless, also an advocate of bill-and-keep, offers a plan that suffers from the same systemic deficiencies as the ICF plan. The detrimental effects of disregarding cost-based pricing and network payment principles are exacerbated even further by the Western Wireless proposal to adopt bill and keep on a more aggressive time schedule than presented in the ICF plan.¹⁶

¹³ See *infra* at Sections II.J.1-2 and II.J.4-5.

¹⁴ *Id.* at Section II.J.3.

¹⁵ *Id.* at Section II.J.6.

¹⁶ *Id.* at Section II.J.7.

Even plans that reject mandatory bill and keep may not correctly recognize basic cost-causation guidelines embodied in the Rural Alliance principle of cost-based pricing for network usage. The principle of cost-based pricing focuses on the adequacy of intercarrier compensation, not just the existence of compensation. Although the Cost-Based Intercarrier Compensation Coalition (“CBICC”) *nominally* adheres to a cost-based principle, its proposed rates for rural areas are insufficient.¹⁷ Failure to establish compensatory intercarrier compensation rates will result in undue pressure on the universal service fund — the sustainability of which is a critical public policy goal. Similarly, although the National Association of State Utility Consumer Advocates (“NASUCA”) appropriately recognizes and supports the principle of payment by network users, the proposal does not necessarily protect against the establishment of non-compensatory rural rates, thus raising the same concerns with rate adequacy and sustainability of the universal service fund.¹⁸

The stability of the universal service fund is a keystone public policy goal and a primary Rural Alliance principle. As noted above, avoiding undue pressure on the universal service fund is critical. Bill-and-keep plans, by eliminating a major element of rate design, inevitably subject the universal service fund to unwarranted pressure. The ICF plan creates undue pressure on the universal service fund in two ways: the plan eliminates an element of cost recovery, and it allows certain companies to reap windfalls from expense reductions resulting from intercarrier compensation reform.¹⁹ The Western

¹⁷ *Id.* at Section II.J.8.

¹⁸ *Id.* at Section II.J.9.

¹⁹ *Id.* at Sections III.E.2-3.

Wireless plan also moves to bill and keep and divorces universal service funding from cost principles, which will result in long-term insufficient funding levels.²⁰ These flaws alone render adoption of either the ICF or Western Wireless plan unwise.

The rate comparability and affordability principles contained in the law also should not be sacrificed in the process of unifying intercarrier rates. Both the ICF and CBICC plans impose additional customer charges to offset intercarrier compensation reductions. By proposing excessive increases in SLCs, the ICF plan exacerbates the disparity between urban and rural customer rates.²¹ CBICC also proposes to offset intercarrier compensation reductions through increases in “end user charge supplements.” Hence, universal service funds will last only as long as necessary to phase in a carrier’s end-user charge supplement at no more than 50 cents per year.

Maintenance of current interconnection rules and points of interconnection within the network is critical to the industry’s stability. By ignoring rural transport costs, the ICF’s “edge” scheme proposes to substitute the existing logical and legal (though often misapplied) interconnection rules with overly complex rules that ignore cost-causation principles.²² The Western Wireless plan impermissibly shifts certain transport obligations to LECs by suggesting an unwarranted new “edge” approach to interconnection obligations.²³ CBICC’s plan illegally suggests that competitive local exchange carriers should be permitted to designate a single point of interconnection

²⁰ *Id.* at Section III.E.4.

²¹ *Id.* at Sections III.E.1 and 5.

²² *Id.* at Sections IV.A.7.(a-g).

²³ *Id.* at Section IV.A.7.h.

within a Local Access and Transport Area (“LATA”), thereby completely ignoring the configuration of RLEC networks.²⁴

As demonstrated in detail herein, the ICF, Western Wireless, CBICC and NASUCA plans each suffer fatal weaknesses.²⁵ Rational intercarrier compensation principles require rejection of these plans for failure to meet legal and policy standards and requirements.

F. The Rural Alliance Recommendations Balance the Need for Change with An Achievable Vision.

The Rural Alliance understands and embraces the changes in the industry, and the resulting need for change in the framework of intercarrier compensation. The changes that the industry is experiencing in both the marketplace and technology, however, do not warrant the proposed imposition of a mandatory bill-and-keep regime as introduced by the Commission in the initial *ICC NPRM*²⁶ and now promoted by a few of the parties in this proceeding.²⁷

²⁴ *Id.* at Section IV.A.7.i.

²⁵ The National Association of Regulatory Utility Commissioners (“NARUC”) also filed a plan with the Commission on May 18, 2005. The Rural Alliance will address aspects of NARUC’s plan in Reply Comments. Considering the magnitude and breadth of the issues before the Commission in this Docket, as well as the volume of anticipated Comments that will be filed, the Rural Alliance respectfully requests that the time period to submit Reply Comments should be extended.

²⁶ *See In the Matter of Developing a Unified Intercarrier Compensation Regime*, CC Docket No. 01-92, Notice of Proposed Rulemaking, (“*ICC NPRM*”) (rel. April 27, 2001) at ¶ 37.

²⁷ *See In the Matter of Developing a Unified Intercarrier Compensation Regime*, CC Docket No. 01-92, Ex Parte Brief of the Intercarrier Compensation Forum in Support of the Intercarrier Compensation and Universal Service Reform Plan Legal Brief, (“*ICF Brief*”) (filed Oct. 5, 2004) at p. 20; and Ex Parte ICC Plan Outline by Western Wireless Corp, (“*Western Wireless Plan*”) (filed Nov. 18, 2004) at p. 2.

The Rural Alliance offers these Comments in an effort to create an achievable and actionable vision, consistent with existing Federal law, whereby consumers in remote and sparsely populated regions of the country can enjoy the benefits of the rapidly evolving telecommunications environment. The Rural Alliance recommendations are summarized below:

Economic Efficiency:

- Any intercarrier compensation mechanism that is adopted should promote economic efficiency, recognizing that all RSPs that use the network should pay for it.
- Traffic-sensitive rates for exchange access and reciprocal compensation should be unified based on embedded costs and in conformance with the Act's additional cost standard.
- Mandatory bill-and-keep plans are inconsistent with statute and should not be adopted.

Balanced cost recovery:

- Balanced cost recovery must be maintained among nationally benchmarked end-user rates, unified intercarrier compensation rates, and the Universal Service Fund ("USF") in order to preserve universal service while limiting unnecessary fund growth.
- Reductions in intercarrier revenues should be offset through USF support or another revenue replacement mechanism.
- SLC caps should be the same for urban and rural customers to ensure rate comparability.

Interconnection:

- Application of the Commission's interconnection rules should be clarified to ensure that network obligations of other carriers are not unfairly imposed on RLECs.

- Exchange access and reciprocal compensation should be maintained, as the law requires.
- Tandem access and transit services are required under a carrier's duty to interconnect and should be provided on a fair, open, and nondiscriminatory basis.
- Rules governing interconnection between CMRS providers and LECs must reflect the statutory obligations of LECs, including interconnection within the LEC's network and toll dialing parity requirements.
- All Carriers Should Be Required to Correctly Identify Terminating Traffic for Billing Purposes.

Jurisdiction:

- Any reforms that are to be legally implemented must involve both State and Federal regulators through a constructive, collaborative process including Joint Board referrals.
- Exchange access and reciprocal compensation cannot be combined, as current law does not give the Commission authority over intrastate access.

IP environment:

- The record in this proceeding must include solutions for ISP-bound traffic as well as investigation of IP interconnection issues to ensure that the transition from the circuit-switched to the IP environment is addressed simultaneously with reforms contemplated in the circuit world.
- ISP traffic bound for or terminated on LEC networks should be subject to exchange access.
- The Enhanced Service Provider ("ESP") exemption from access for ISP-bound traffic applies only to ISPs directly connected to a LEC.
- IP reforms must include fair and open interconnection standards between independent ISPs and large backbone providers as well as a Joint Board referral for a new IP high-cost support paradigm.

Throughout the subsequent phases of this proceeding, the Rural Alliance looks forward to providing additional substantive analysis, responses and further refinements of proposals consistent with the Rural Alliance principles, the law, regulations and public policy that foster universal service and the deployment of advanced technology in the nation's rural and high-cost service areas.

II. INTERCARRIER COMPENSATION SHOULD BE STRUCTURED TO PROMOTE ECONOMIC EFFICIENCY BY BALANCING EFFICIENCY CONSIDERATIONS.

One of the Commission's goals for intercarrier compensation reform is that an intercarrier compensation regime should promote economic efficiency.²⁸ Specifically, the Commission indicates that any new approach should encourage the efficient use of, and investment in, telecommunications networks, as well as the development of efficient competition.²⁹

The National Association of Regulatory Utility Commissioners ("NARUC") has also adopted several principles relating to the promotion of economic efficiency through the proper structuring of intercarrier compensation.³⁰ The Rural Alliance believes that its

²⁸ See *ICC NPRM* at ¶ 31.

²⁹ *Ibid.*

³⁰ See National Association of Rural Utility Commissioners ("NARUC") Study Committee on Intercarrier Compensation Goals for a New Intercarrier Compensation System, (*"NARUC Principles"*) (rel. May 5, 2004):

- II.A. An integrated intercarrier compensation plan should encompass rates for interconnecting CLEC and ILEC local traffic as well as access charges paid by interexchange carriers ("IXCs").
- II.B. CLECs, IXCs, ISPs, VoIP, wireless, and any other companies exchanging traffic over the Public Switched Telecommunications Network should be covered. ("Covered Entities")
- III.A. The compensation plan should minimize arbitrage opportunities and be resistant to gaming.
- III.B. Intercarrier compensation should be designed to recover an appropriate portion of the requested carrier's applicable network costs. At a minimum, this will require compliance with the jurisdictional separations and cost allocation rules, applicable case law in effect at any point in time, and 47 U.S.C. 254(k).
- III.C. A carrier that provides a particular service or function should charge the same amount to all Covered Entities to whom the service or function is being provided. Charges should not discriminate among carriers based on: the classification of the requesting carrier; the classification of the requesting carrier's customers; the location of the requesting carrier's customer; the geographic location of any of the end-users who are parties to the communication; or the architecture or protocols of the requested carrier's network or equipment.
- III.D. Intercarrier compensation charges should be competitively and technologically neutral and reflect underlying economic cost.
- III.E. The intercarrier compensation system should encourage competition by ensuring that requested carriers have an economic incentive to interconnect, to carry the traffic, and to provide high-quality service to requesting carriers. In limited circumstances, carriers may voluntarily enter into a bill and keep arrangement.
- III.F. Volume of use should be considered when setting intercarrier compensation rates. Available capacity may be used as a surrogate for volume of use.

recommendations are consistent with the NARUC principles and will best allow for an economically efficient intercarrier compensation regime, as explained below.

A. A Mandatory “Bill and Keep” Regime Is Contrary to both Established Law and Rational Policy.

The Commission has recognized repeatedly that incumbent local exchange carriers (“ILECs”), including those with the characteristics of the members of the Rural Alliance should be permitted to establish rates for interstate access services that recover their costs.³¹ Moreover, the Commission has also indicated its understanding that end-user customers should not pay rates that unreasonably support services provided to other customers.³² The Rural Alliance respectfully submits that a mandatory bill-and-keep regime is contrary to these principles, inconsistent with the established underlying policy and in conflict with the plain meaning of the Communications Act of 1934, as amended (the “Act”).

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- III.G. Any intercarrier compensation system should be simple and inexpensive to administer.
 - IV. Market-based rates should be used where the market is determined to be competitive. A rigorous definition of “competitive market” is needed in order to prevent abuses.
 - VII.B. A new intercarrier compensation system should recognize that areas served by some rural local exchange carriers are significantly more difficult to serve and have much higher costs than other areas.

³¹ See *In the Matter of Multi-Association Group (“MAG”) Plan for Regulation of Interstate Services of Non-Price Cap Incumbent Local Exchange Carriers and Interexchange Carriers*, CC Docket No. 00-256, *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, *Access Charge Reform for Incumbent Local Exchange Carriers Subject to Rate-of-Return Regulation*, CC Docket No. 98-77, and *Prescribing the Authorized Rate of Return for Interstate Services of Local Exchange Carriers*, CC Docket No. 98-166, Second Report and Order and Further Notice of Proposed Rulemaking in CC Docket No. 00-256, Fifteenth Report and Order in CC Docket No. 96-45, and Report and Order in CC Docket Nos. 98-77 and 98-166, FCC 01-304 (“MAG Order”) (rel. Nov. 8, 2001) at ¶¶ 12, 84, and 206.

³² *Id.* at ¶¶ 18, 23, and 43. The discussions cited address concern about “subsidization” between high-volume toll users and low-volume toll users. The Rural Alliance is especially concerned that the outcome of this proceeding does not create subsidization of urban interstate network users by the rural end-user subscribers and the rural carriers that serve them. This result would be contrary to existing law, rules, and practice.

While many parties profess that the “cost causer” should pay the costs, some of the same parties attempt to shirk responsibility for the payment of joint and common costs that are a necessary element of the telecommunications services those parties provide. As a matter of policy and law, the Commission has always recognized that both carriers and their customers benefit from utilization of the rural Local Exchange Carriers (“RLECs”) network to originate and terminate telecommunications.

Fundamental to the establishment of rational rate structures for any RLEC is the concept of jurisdictional and service allocation of joint and common costs. While the jurisdictional and service cost allocation rules (set forth, respectively, in Parts 36 and 69 of the Commission’s Rules) appear complicated, the fundamental concepts are easily understood. The plant, and associated expenses, generally required for the provision of basic telephone service is utilized by customers to make and receive all forms of communications including local, intrastate non-local, interstate and international. While the establishment of connectivity to the nationwide switched telephone network is of benefit to the customer ordering the connectivity, it is a fundamental ratemaking principle that all others who can use the same plant to call and be called by the customer also benefit.

This basic and essential principle is grounded in established policy and law that cannot be overlooked or overturned in this proceeding. The fundamental concept of jurisdictional cost allocation ensures that joint and common costs are reasonably allocated on a jurisdictional basis, and that rates are established for each jurisdictional

service to recover the apportioned costs.³³ The Commission has always recognized that costs should be assigned, where possible, to those customers who benefit from the services provided by the network.³⁴ Regardless of jurisdiction, it has been the policy of the Commission and the states to allocate joint and common costs to all telecommunications users.

The prescription of a mandatory bill-and-keep regime would prohibit a reasonable cost allocation that reflects a rational measure of the network use of other carriers and their customers. Failure to permit the application of charges to those carriers and their customers who utilize networks to originate and terminate telecommunications will inevitably lead to a recovery of the associated costs from alternative sources, thereby inappropriately subsidizing the services of those carriers that interconnect to and use local exchange carrier (“LEC”) networks.

The Rural Alliance recognizes that the Act specifically provides for the *possible* use of a bill and keep arrangement.³⁵ The Act does not, however, permit *mandatory* application of bill and keep to any form of interconnection. In the context of a reciprocal compensation arrangement, the Act does not allow the Commission to preclude bill-and-keep arrangements when the parties “waive mutual recovery.” Rural Alliance members will not waive their rights to establish rates for services that recover their costs, including an appropriate portion of the joint and common costs necessary to operate their networks.

³³ See Smith v. Illinois Bell, 282 U.S. 133 (1930).

³⁴ See *MAG Order* at ¶ 43, citing 12 FCC Rcd at 16013 ¶ 77. (“*Access Charge Reform Order*”)

³⁵ 47 U.S.C. § 252(d)(2)(B).

B. The Commission Cannot Forbear from Act Provisions to Impose Mandatory Bill and Keep.

The Federal Communications Commission (“Commission”) seeks comment on whether it could use its authority under section 10 of the Act to forbear from certain aspects of the compensation requirement of section 251(b)(5) as part of any intercarrier compensation reform effort.³⁶ Specifically, the Commission asks whether it could exercise forbearance to impose a bill-and-keep regime.³⁷ The Rural Alliance believes that the Commission should not seek to exercise its forbearance authority to impose a bill-and-keep regime, as to do so would actually thwart the Commission’s stated goal of promoting economic efficiency through intercarrier compensation reform. Even if economic efficiency could be achieved under bill and keep, the Rural Alliance does not believe that the forbearance criteria would be satisfied with respect to the section 251(b)(5) compensation requirement.

Section 10 of the Act allows the Commission to forbear from applying any regulation or any provision of the Act to a telecommunications carrier or telecommunications service if the Commission determines that the following three conditions are met:

1. enforcement of such regulation or provision is not necessary to ensure that the charges, practices, classifications, or regulations by, for, or in connection with that telecommunications carrier or telecommunications service are just and reasonable and are not unjustly or unreasonably discriminatory;
2. enforcement of such regulation or provision is not necessary for the protection of consumers; and

³⁶ *FNPRM* at ¶ 74.

³⁷ *Ibid.*

3. forbearance from applying such provision or regulation is consistent with the public interest.³⁸

In the absence of a factual record demonstrating that each of these criteria is fulfilled, forbearance is inappropriate. The factual circumstances of the market areas served by Rural Alliance members are inconsistent with the statutory criteria required for the Commission to forbear from the application of the interconnection pricing standards established pursuant to the Act.

The costs allocated to interstate interexchange access services are established pursuant to the Commission's Rules. Forbearance from the application of these rules and the resulting charges will inevitably shift cost recovery from rates charged to one class of carrier and its customers to other revenue sources, thereby creating unjust discrimination. In addition, continued enforcement of the current regulations providing for the payment of reciprocal compensation for transport and termination is also necessary to protect consumers. Without such charges, consumers may be forced to pay the costs of terminating calls for which they were not responsible. To the extent that this potential forbearance results in unreasonable additional charges on one class of consumers while unreasonably reducing charges on other consumers who use the rural networks, the potential forbearance would not only be discriminatory, but also inconsistent with the Commission's general charge to protect consumers and the public interest.

Continued enforcement of these same regulations is also consistent with the public interest in terms of economic efficiency. If all consumers and all carriers do not pay the costs associated with their use of a telecommunications network, it is highly

³⁸ 47 U.S.C. § 10(a).

unlikely that economic efficiency will result, since there will be network costs that are not be paid by the cost causers. For all of the above reasons, the Commission should not forbear from application of the section 251(b)(5) compensation requirement.

In the Further Notice of Proposed Rulemaking (“*FNPRM*”), the Commission seeks comment on “whether the bar to forbearance contained in section 10(d) precludes exercise of forbearance in this case. On its face, section 10(d) precludes forbearance only until section 251(c) is implemented and is silent with respect to obligations imposed under section 251(b).”³⁹ The silence with respect to section 251(b) is not relevant to the inquiry. As discussed previously, the forbearance criteria are not met for the areas served by the Rural Alliance members and other RLECs. Consequently, with respect to rural companies, the issue regarding section 10(d) raised by the *FNPRM* is neither reached nor relevant.

The Commission’s question concerning whether section 251(b)(5) of the Act is or is not included within 251(c) is misplaced. Specifically, the Commission states:

We note, however, that the predecessor to the Wireline Competition Bureau previously held that section 251(b) obligations are incorporated by reference into section 251(c). Was this holding correct and, if not, should the Commission take this opportunity to reverse it?⁴⁰

The cited section of the *FNPRM* is incorrect, however, to the extent that it concludes that the Common Carrier Bureau “held” that the section 251(b) obligations are incorporated by reference into section 251(c). The Bureau did indeed state:

³⁹ *FNPRM* at ¶ 76.

⁴⁰ *Ibid.*

Section 251(b) is incorporated explicitly into section 251(c) at the outset of that subsection, however, and further in the subsection establishing a duty for incumbent LECs to negotiate agreements in good faith.⁴¹

The context of the statement was in consideration of whether certain merger conditions imposed on a carrier required that carrier to permit all of the terms and conditions of its interconnection arrangements with a carrier in one State to be used by a carrier in another State. Because the section 251(b) conditions had originally been negotiated by a non-rural carrier subject to section 251(c), the Bureau concluded that the applicable merger conditions did apply to all of the terms and conditions in its interconnection arrangement. For purposes of the specific matter before the Bureau section 251(b) interconnection terms were incorporated into a section 251(c) good faith negotiation. The Bureau, however, did not hold generally that section 251(b) was fully incorporated within section 251(c). Consequently, there is no reason or basis to reverse a “holding” that does not exist.

There is a fundamental principle of statutory interpretation that gives meaning to every portion of a statute. In another instance where the Commission considered the proposition that section 251(b)(5) was “incorporated” within section 251(a) of the Act, it rejected the proposition, stating:

Otherwise, section 251(b)(5) would cease to have independent meaning, violating a well-established principle of statutory construction requiring

⁴¹ See *In the Matter of Application of GTE Corp., Transferor, and Bell Atlantic Corp., Transferee, For Consent to Transfer Control of Domestic and International Sections 214 and 310 Authorizations and Application to Transfer Control of a Submarine Cable Landing License*, CC Docket No. 98-184, Letter from Carol Matthey, Deputy Chief, Common Carrier Bureau, to Michael L. Shor, Swidler Berlin Shereff Friedman, 16 FCC Rcd 22, 23 (Comm. Car. Bur. 2000).

that effect be given to every portion of a statute so that no portion becomes inoperative or meaningless.⁴²

As shown previously, forbearance criteria are not met for rural companies. Even if the Commission were to wrongly conclude that the forbearance criteria were met, forbearance with respect to the pricing standard applicable to section 251(b)(5) reciprocal compensation could not provide a sustainable basis to forbear from the pricing rules for other interconnection services. For non-rural carriers, other sections of the Act and the associated rules of the Commission govern the provision of other interconnection services.⁴³ Accordingly, the Rural Alliance respectfully submits that no legal or factual basis exists upon which the Commission could lawfully forbear from enforcement of any provision of the Act to mandate the involuntary imposition of a bill-and-keep intercarrier compensation regime on any carrier.

C. Economic Efficiency Will Not Be Achieved if Services Are Not Priced Appropriately.

Economics seeks to promote consumer welfare by allocating scarce resources in a world with unlimited wants. To allocate resources, prices are assigned to goods and services. As demonstrated more fully in Appendix B, if prices are not set to accurately reflect the cost of producing a good or service, economic efficiency will not be

⁴² See *In the Matter of Total Telecommunications Services, Inc. and Atlas Telephone Company, Inc. v. AT&T*, File No. E-97-003, Memorandum Opinion and Order, (rel. Mar. 13, 2001) at ¶ 26. The FCC's interpretation was affirmed in *AT&T Corporation v. FCC*, 317 F.3d 227 at 235. (D.C. Cir. 2003).

⁴³ See, e.g., 47 U.S.C. § 251(c)(2)(A) which addresses "the transmission and routing of telephone exchange service and access service." See also 47 U.S.C. § 10(d) which states that the Commission cannot forbear until it determines that the requirements of § 251(c) have been fully implemented.

achieved.⁴⁴ Rather than requiring only end users who order a network connection to pay, the Rural Alliance believes that requiring payment for network usage from all network users, including other carriers, will promote economic efficiency, as network demand will be based on the cost of using the network.⁴⁵

Mandating a bill-and-keep regime for all Public Switched Telephone Network (“PSTN”) traffic⁴⁶ will force carriers to enter into bill-and-keep agreements, who otherwise would not enter into such arrangements. There are some reciprocal compensation situations in which bill and keep is appropriate and generally will voluntarily be negotiated by carriers in those contexts.⁴⁷ For example, when traffic is in balance and each carrier’s costs are similar, a voluntary bill-and-keep arrangement could be negotiated.

With respect to access charges, the Commission asks whether it should adopt mechanisms to offset revenues previously recovered if it reduces or eliminates the ability of LECs to impose access charges on interexchange carriers (“IXCs”).⁴⁸ The Rural

⁴⁴ See *infra* at Appendix B

⁴⁵ See NARUC Principles:

- III.B. Intercarrier compensation should be designed to recover an appropriate portion of the requested carrier’s applicable network costs; intercarrier compensation charges should reflect underlying economic cost.
- III.C. The intercarrier compensation system should encourage competition by ensuring that requested carriers have an economic incentive to interconnect, to carry the traffic, and to provide high-quality service to requesting carriers.

⁴⁶ The *FNPRM* does not address compensation for exchanges of traffic over the Internet, such as between ISPs and backbone providers. Nevertheless, when this traffic uses the PSTN to originate or terminate calls, the Rural Alliance believes such traffic necessarily must be addressed in this proceeding, as well as in the IP Enabled Services docket.

⁴⁷ Interexchange traffic carried by IXCs is not an instance where bill and keep would voluntarily be negotiated.

⁴⁸ See *ICC NPRM* at ¶¶ 99, 108, and 114.

Alliance believes that before answering this question, a more fundamental question should be asked: “Should access charges be eliminated?” The short answer is “No.” Access charges should only be eliminated when access service is *de minimus* and IXC’s are no longer providing end-to-end long distance. Even for non-rural companies the price of access should not be zero, since the cost is not zero and the structure of the retail-wholesale relationship precludes a fair application of bill and keep. Thus, the Rural Alliance believes that access charges must be maintained for both rural and non-rural LECs.

D. Embedded Costs Should Be Used to Set Intercarrier Compensation Rates.

Two terms are generally used to describe the data used to perform cost calculations – forward looking and embedded. Each of these is a current measure of cost because each is calculated as of today. Embedded cost uses accounting records reflecting historical costs to measure today’s cost, while forward-looking cost uses current technology, input prices and industry procedures to measure today’s cost.

Unlike embedded costs, which are circumscribed by both Commission rules and by the accounting industry’s Generally Accepted Accounting Principles, forward looking costs are subject to much more interpretation and are not observable. Because of these various interpretations, there is generally more disagreement as to how forward-looking costs should be calculated. Moreover, forward-looking costs are merely estimates. Some parties to cost proceedings have even suggested that technologies in testing or development should be used to determine forward-looking cost, yet the Commission’s rules clearly indicate that “telecommunications technology currently available” should be

applied.⁴⁹ Thus, in some instances, a *speculative cost*, not based on technology or operating procedures generally employed today, is being misconstrued as forward-looking cost.

Embedded costs and forward-looking costs will differ to the extent that technology, input prices, and industry procedures have changed over time.⁵⁰ If technology allows a service to be provided more efficiently and/or input prices are declining, forward-looking costs will be lower than embedded costs. Conversely, if technology is not becoming more efficient for the provision of a given service, and/or input prices are increasing, forward-looking costs will be equal to or greater than embedded costs.⁵¹ Since embedded costs reflect past technology and input prices, embedded costs will trend in the same direction as forward-looking costs over the long run.

Forward-looking costs will differ from embedded costs because of technology improvements in the provision of a given service, input price changes and facility utilization. If technology causes progressive improvements in efficiency, embedded costs

⁴⁹ In its rules to develop costs for unbundled network elements the Commission specified that “[t]he total element long-run incremental cost of an element should be measured based on the use of the most efficient *telecommunications technology currently available* and the lowest cost network configuration, given the existing location of the incumbent LEC’s wire centers.” 47 C.F.R. § 51.505(b)(1), emphasis added.

⁵⁰ Other factors, such as prescribed depreciation lives of assets, will cause embedded costs and forward-looking costs to differ. For example, since regulatory agencies may wish to maintain lower rates for services whose rates depend upon the calculation of a revenue requirement, depreciable asset lives used for calculating embedded costs, may be longer than asset lives that would be assumed in a forward-looking cost calculation. Differences between forecasted and actual demand and plant utilization may also cause embedded and forward-looking cost calculations to diverge.

⁵¹ The Iowa Utilities Board argued that, in Iowa at least, embedded costs were lower than FLEC. *See In the Matter of the Implementation of the Local Competition Provisions of the Telecommunications Act of 1996*, CC Docket No. 96-98, Iowa Utilities Board Motion for Stay of Implementation of the Local Competition Provisions of the Telecommunications Act of 1996, (filed Sept. 18, 1996) at p. 9.

will trend in the same direction as forward-looking costs, except that embedded cost decreases will lag forward-looking cost decreases. On the other hand, input prices in times of inflation will result in forward-looking costs being higher than embedded costs. For example, labor costs and associated benefit costs appear to be ever increasing; and since labor cost is a significant proportion of total cost, input prices may be higher on a forward-looking basis than on an embedded basis. Finally, in an industry with significant fixed costs, unit costs will increase as intermodal competition forces facility utilization rates to fall. Consequently, labor and facility utilization cost increases in many cases will offset efficiency gains resulting from technological improvements; thus, the overall difference between forward-looking and embedded costs will be minimal.

Given that the forward-looking and the embedded cost of reciprocal compensation and access services are not likely to be substantially different, the use of embedded costs is not only justifiable but also preferable. The Commission's experience with estimating forward-looking costs clearly demonstrates not only the limits of accurately projecting forward-looking costs but also the significant administrative burden associated with forward-looking costs.

Experts have argued that the considerable administrative cost of calculating forward-looking costs, including the costs of running the Commission's Synthesis model for non-rural companies may not be worth the effort. In fact, former Commissioner Furchtgott-Roth and other economists have questioned whether the model should even be used all to calculate absolute support levels:

...the model is good at evaluating relative costs — i.e. whether it costs more to provide service to residents of rural Montana than to residents of Minneapolis or even downtown Missoula — even if the model is not as

good at determining absolute costs — i.e., how much it actually costs to provide service to a resident in either rural Montana or downtown Missoula. The problem is that it is the latter purpose — determining an absolute cost of providing service to these areas and basing Federal support on some percentage of that amount — for which this agency seem intent on using the models.⁵²

The model is also completely dependent on hundreds of assumptions about the local exchange markets and costs. The bottom line is that, simply by making different assumptions about local exchange networks, or by picking different input values for costs, the Commission is able to push the end result in whatever direction it chooses. I do not believe that a system that can be manipulated in this way will generate the “specific” and “predictable” universal service support that the 1996 Act requires. In addition, the fact that the Commission has found it necessary to tinker with this model so extensively reflects its fundamental lack of confidence in its model.⁵³

The cost of administering the model for non-rural companies is significant. One of the reasons that the model was not supported by former Commissioner Furtchgott-Roth, the only economist on the Commission at the time, was that the costs of modeling forward-looking costs outweighed the benefits:

The Commission’s Model Is Unwieldy, Easily Manipulated, and Will Require Constant Maintenance. Not only does the Commission have its universal service priorities wrong, but also the model on which it relies is inconsistent with the Telecommunications Act’s requirement that universal service support be “specific” and “predictable.” The model is an immensely complicated computer program that requires around 180 hours - more than one week - to run. In the course of this proceeding, the Commission has made numerous changes to the model platform, and each change has required interested parties to go back to their computers and spend days testing the model. ... The model is also going to be

⁵² *In the Matter of Federal-State Joint Board on Universal Service*, CC Docket No. 96-45 and *Forward-Looking Mechanism for High-Cost Support for Non-Rural LECs*, CC Docket No. 97-160, Fifth Report and Order, Separate Statement of Commissioner Harold Furtchgott-Roth, FCC 98-279 (rel. Oct. 28, 1998) at p. 1.

⁵³ *In the Matter of Federal-State Joint Board on Universal Service*, CC Docket No. 96-45 and *Forward-Looking Mechanism for High-Cost Support for Non-Rural LECs*, CC Docket No. 97-160, Tenth Report and Order, Separate Statement of Commissioner Harold Furtchgott-Roth, FCC 99-304 (rel. Nov. 2, 1999) at p. 2.

enormously time-consuming and expensive to maintain. Each time technology or prices change, the Commission's staff will be required to adjust the model. I am opposed to wasting resources on this effort.⁵⁴

For rural companies, the considerably higher administrative expense related to obtaining forward-looking costs verses embedded costs does not merit the use of forward-looking cost in lieu of embedded cost.

Cost proxy models, which are the primary tools available to calculate forward-looking costs, have proven unreliable in estimating costs for rural companies. The Commission developed a forward-looking cost proxy model for use in determining universal service support for non-rural companies.⁵⁵ The Commission indicated that it would use such a model to determine support for rural carriers "only when we have sufficient validation that forward-looking support mechanisms for rural carriers produce results that are sufficient and predictable."⁵⁶ To "assist in identifying the issues unique to rural carriers and analyze the appropriateness of proxy cost models for rural carriers,"⁵⁷ the Federal-State Joint Board on Universal Service recommended, and the Commission approved, the creation of a Rural Task Force ("RTF").⁵⁸ The RTF began its work in July of 1998, and issued its final Recommendation to the Joint Board in September of 2000. One of the RTF's major policy recommendations was that "the Synthesis Model not be

⁵⁴ *Ibid*

⁵⁵ See *In the Matter of Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, and *Forward-Looking Mechanism for High-Cost Support for Non-Rural LEC*, CC Docket No. 97-160, Fifth Report and Order, FCC 98-279 (rel. Oct. 28, 1998).

⁵⁶ See *Federal-State Joint Board on Universal Service*, CC Docket 96-45, Report and Order, FCC 97-157 (rel. May 8, 1997) at ¶ 252.

⁵⁷ *Id.* at ¶ 253.

⁵⁸ "Federal-State Joint Board on Universal Service Announces the Creation of Rural Task Force: Solicits Nominations for Membership on the Rural Task Force." Public Notice, FCC 97J-1 (rel. Sept. 17, 1997).

used for determining the forward-looking costs of rural carriers.”⁵⁹ In making this recommendation, the RTF summarized its conclusions from a rigorous study by stating:

The aggregate results of this study suggest that, when viewed on an individual wire center or individual rural carrier basis, the costs generated by the Synthesis Model are likely to vary widely from reasonable estimates of forward-looking costs. As a result, it is the opinion of the Task Force that the current model is not an appropriate tool for determining forward-looking cost of rural carriers.⁶⁰

According to the RTF, the “Law of Large Numbers” suggests that those wire centers where the estimated costs are too high will offset those where estimated costs are too low, resulting in a reasonable overall result.⁶¹ Because rural companies do not have thousands of wire centers over which to average results, errors in the rural cost calculation for a few wire centers may not be “averaged out.” Thus, the overall forward-looking cost for a rural company may be significantly in error.

In addition, the Commission has indicated that its Total Element Long-Run Incremental Cost (“TELRIC”) methodology used to determine Unbundled Network Elements (“UNE”) prices may not be functioning as intended, due in part to the hypothetical nature of the calculation. In September of 2003, the Commission issued a Notice of Proposed Rulemaking seeking comment on its TELRIC methodology, in which the Commission made the following statements:

⁵⁹ See *In the Matter of Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Rural Task Force Recommendation to the Federal-State Joint Board on Universal Service, (“RTF Recommendation”) (rel. Sept. 29, 2000) at p. 4.

⁶⁰ *Id.* at p. 18.

⁶¹ See *Rural Task Force White Paper #4, A Review of the FCC’s Non-Rural Universal Service Fund Method and the Synthesis Model for Rural Telephone Companies*, (“RTF White Paper #4”) (rel. Sept. 2000) at pp. 7-8.

- To the extent that the application of our TELRIC pricing rules distorts our intended pricing signals by understating forward-looking costs, it can thwart one of the central purposes of the Act: the promotion of facilities-based competition.⁶²
- We tentatively conclude that our TELRIC rules should more closely account for the real-world attributes of the routing and topography of an incumbent's network in the development of forward-looking costs.⁶³
- The UNE pricing methodology, while forward-looking, must be representative of the real world and should not be based on the totally hypothetical cost of a most-efficient provider building a network from scratch.⁶⁴
- We ask parties to discuss whether a regime focused more closely on the existing network of an incumbent LEC would be easier for State commissions to implement than the current TELRIC regime.⁶⁵

None of the identified problems has been resolved in the Commission's Synthesis Model.

Given the documented deficiencies of forward-looking cost proxy models,⁶⁶ such models should not be used to determine rural prices for reciprocal compensation and access services without substantial revision. The Rural Alliance believes that to adequately revise the Commission's Synthesis Model, or any other forward-looking cost proxy model, for rural companies will not be cost effective. The Commission has already noted that model inputs do not adequately reflect rural carriers' costs.⁶⁷ Capturing

⁶² See *In the Matter of Review of the Commission's Rules Regarding the Pricing of Unbundled Network Elements and the Resale of Services by Incumbent Local Exchange Carriers*, WC Docket No. 03-173, Notice of Proposed Rulemaking, FCC 03-224 ("TELRIC NPRM") (rel. Sept. 15, 2003) at ¶ 3.

⁶³ *Id.* at ¶ 52.

⁶⁴ *Id.* at ¶ 53.

⁶⁵ *Id.* at ¶ 60.

⁶⁶ The RTF conducted a thorough review of the Synthesis Model in particular because this model was judged to be the best by the Commission for the purpose of determining universal service costs and support amount for non-rural companies.

⁶⁷ See *In the Matter of Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, *Multi-Association Group Plan for Regulation on Interstate Services of Non-Price Cap Incumbent Local Exchange Carriers and Interexchange Carriers*, CC Docket No. 00-256, Fourteenth Report and Order in CC Docket

accurate input data is but one of the many revisions necessary to develop accurate results for rural companies. As the RTF documented, the plant placed by the Synthesis Model varied widely from actual plant in service.⁶⁸ Possible reasons for this discrepancy include inaccurate or non-existent information on rural customer locations and inaccurate data on terrain and soil type. Clearly the resource expenditure necessary to refine a forward-looking cost proxy model to produce credible rural results is enormous given the years and resources devoted to developing the Benchmark Cost Proxy Model and the HAI (formerly known as “Hatfield”) Model, which the Commission then refined and combined into the Synthesis Model. Even after such an effort, a proxy model would not address the Commission’s concerns regarding the hypothetical nature of these costs and the impact on its current TELRIC rules.

In addition to the difficulties of developing reasonable estimates for rural forward-looking costs, if the use of forward-looking cost estimates will produce results that are significantly lower than embedded costs, dynamic efficiency will not be achieved.⁶⁹ If rates based on forward-looking cost estimates do not allow a LEC to recover the costs of efficient investments made in the past, LECs will be less likely to invest in technologies that may become obsolete before the asset is fully depreciated. This reluctance to invest would harm customers, as they would be deprived of services available through improved technology.

No. 96-45, and Report and Order in CC Docket No. 00-256, FCC 01-157 (“*RTF Order*”) (rel. May 23, 2001) at ¶ 5.

⁶⁸ The RTF’s analysis of the Synthesis Model found that it generally overestimated the amount of aerial and underground plant, while it underestimated the amount of buried plant. *See RTF White Paper #4* at p. 9.

⁶⁹ *See infra* at Appendix B for a discussion of dynamic efficiency in “The Economic Cost of Mandatory Bill and Keep” at p. 6 by Dale Lehman.

E. Use of Embedded Costs Will Comply with the Additional Cost Standard.

The Commission seeks comment on whether to replace current rules with an incremental cost standard to set intercarrier compensation rates that comply with the additional cost standard under section 252(d)(2).⁷⁰ The Rural Alliance believes that in order to set unified intercarrier compensation rates for access and reciprocal compensation and meet the additional cost standard, those rates should use embedded costs to determine the average incremental cost of the service plus an allocation of joint and common costs. Use of this methodology provides an appropriate framework to unify reciprocal compensation reciprocal compensation and exchange access pricing, yet maintains consistency with existing jurisdictional and access cost allocations contained in the Commission's rules. Pricing intercarrier compensation in this manner will also promote economic efficiency, as it will send appropriate economic signals to users regarding the costs of originating and terminating telecommunications traffic.

Incremental cost is the change in cost caused by *any* change in output, holding constant the remaining output of the firm. While the generic term incremental cost refers to all ranges of changes in output, there are definitions of incremental cost that refer to specific increments of output. For example, the total incremental cost of a service is the cost avoided by discontinuing an *entire* service, holding constant the production levels of all other services offered by a firm. Marginal cost, another measurement of incremental cost, refers to the additional cost avoided by decreasing the production volume of a service by a *single unit*, holding constant the production levels of all other products and

⁷⁰ FNPRM at ¶¶ 71-73.

services offered by the firm. Average incremental cost of a service is the total incremental cost of a single service per unit of output. In other words, the average incremental cost of a service is the total incremental cost of a service divided by the total units of the service produced.

The Commission currently utilizes Forward-Looking Economic Cost (“FLEC”) as its pricing standard for developing interconnection rates, UNEs and reciprocal compensation. By setting rates using the average incremental cost of a service, plus a reasonable allocation of joint and common costs, the Rural Alliance proposes a similar average incremental cost structure, to that adopted by the Commission in establishing its TELRIC rules:

. . . the total quantity of the facilities and functions that are directly attributable to, or reasonably identifiable as incremental to, such element, calculated taking as a given the incumbent LEC’s provision of other elements.⁷¹

Using the aforementioned structure, embedded costs should be used as an input for reasons described earlier in this filing.

In developing the pricing rules for reciprocal compensation and UNEs, the Commission indicated that “[n]ew entrants should make their decisions whether to purchase unbundled elements or to build their own facilities based on the relative economic costs of these options.”⁷² The decision to purchase access services or reciprocal compensation services from an ILEC is based on whether a carrier can

⁷¹ 47 C.F.R. § 51.505.

⁷² See *Implementation of the Local Competition Provisions in the Telecommunications Act of 1996*, CC Docket No. 96-98 and *Interconnection Between Local Exchange Carriers and Commercial Mobile Radio Service Providers*, CC Docket No. 95-185, First Report and Order, FCC 96-325, (“*Local Competition Order*”) (rel. Aug. 8, 1996) at ¶ 620.

purchase such services from the ILEC at a lower rate than the carrier could build or lease facilities.⁷³ When a carrier determines whether it is more economical to build facilities or buy services from an ILEC, the carrier examines the cost to build facilities over the entire or *total increment* of demand necessary to furnish the service, as the carrier would need to build facilities to accommodate the total demand. Since marginal cost is the cost of the last unit of production, not the cost of producing one unit of a particular product, the Rural Alliance asserts that average incremental cost,⁷⁴ not marginal cost, is the more appropriate standard for intercarrier compensation rate setting.

In requesting comments on the appropriateness of using incremental costs for establishing additional costs, the Commission correctly acknowledges that “[t]he costs that are considered incremental will vary greatly depending on the size of the increment.”⁷⁵ Because at various times carriers may request different increments of a service, the only way a consistent cost measurement can be derived is to measure cost over the total increment of a service demanded. Unlike average incremental cost, marginal costs for services subject to “lumpy” investments may be significantly different depending on the chosen point on the cost curve. For example, if a switch has sufficient capacity to handle one additional call, the marginal cost may be near zero. When the

⁷³ *Ibid.* “Moreover, there is some substitutability between the new entrant’s use of unbundled network elements for transporting traffic and its use of transport under section 252(d)(2). Depending on the interconnection arrangements, carriers may transport traffic to the competing carrier’s end offices or hand traffic off to competing carriers at meet points for termination on the competing carriers’ networks. Transport of traffic for termination on a competing carrier’s network is, therefore, largely indistinguishable from transport for termination of calls on a carrier’s own network. Thus, we conclude that transport of traffic should be priced based on the same cost-based standard, whether it is transport using unbundled elements or transport of traffic that originated on a competing carrier’s network.”

⁷⁴ An allocation of joint and common costs should be added to the average incremental cost.

⁷⁵ See *Local Competition Order* at ¶ 675.

switch does not have sufficient capacity to handle an additional call, the marginal cost would be the cost attributable to adding capacity or upgrading the switch such that it could process the additional call. In this case, the cost of additional capacity could be hundreds or thousands of dollars. Given this cost variability, the Commission should continue the use of total incremental cost to develop an average incremental cost,⁷⁶ as was originally ordered for the pricing of interconnection, UNEs and reciprocal compensation.

The Commission has recognized in the past, that it is also critical that joint and common costs be included in rates. The Commission's FLEC pricing standard for interconnection, UNEs and reciprocal compensation included a reasonable allocation of forward-looking common costs in addition to TELRIC.⁷⁷ The Commission acknowledged that pricing without an allocation of joint and common costs would not allow a carrier to recover the total costs of operating a network.⁷⁸ For example, the Commission observed in setting rates under section 252(d)(2):

Rates for termination established pursuant to a TELRIC-based methodology may recover a reasonable allocation of common costs. A rate equal to incremental cost may not compensate carriers fully for transporting and terminating traffic when common costs are present. We therefore reject the argument of some commenters that "additional costs" may not include a reasonable allocation of forward-looking common costs.⁷⁹

⁷⁶ Average incremental cost is the total incremental cost divided by the total units of output of a good or service.

⁷⁷ 47 C.F.R. § 51.505(a).

⁷⁸ See *Local Competition Order* at ¶ 694.

⁷⁹ *Id.* at ¶ 1058.

In its summary of comments, the Commission indicated that commenters providing rationale for including joint and common costs in the pricing of interconnection, UNEs, and reciprocal compensation noted that:

incumbent LECs should be permitted to recover some measure of forward-looking joint and common costs. These commenters argue that pricing at incremental cost without joint and common costs is economically inefficient because it permits competitors to offer the incumbent LECs' services without making a contribution to common costs that the LECs incur in offering the service. They further contend that excluding recovery of joint and common costs will distort technological decisions because the LEC is encouraged to invest in less efficient technologies that have higher incremental costs and lower common costs, which would tend to destroy economies of scope.⁸⁰

The Rural Alliance believes that the Commission's decision to include some measure of joint and common cost is valid. Prices must include an allocation of joint and common costs in order to entice firms to invest in infrastructure and to comply with statute.⁸¹ If prices do not include an allocation of joint and common cost, there would be a disincentive for new firms to ever invest in their own facilities. Eventually, the firm providing access would go out of business because it would have unrecovered costs.

The Commission also requests comment on whether it should interpret the "additional cost" standard to be the difference between long-run forward-looking total network cost⁸² and the cost of a network with the same number of subscribers in the same

⁸⁰ *Id.* at ¶ 643.

⁸¹ 47 U.S.C. § 254(k).

⁸² Cost definitions are usually tied to a period of time over which cost measurement is performed. The period of time is not fixed, rather, it is a conceptual period of time depending upon the types of adjustments that a firm is able to make in the amounts of the resources it uses. Two measures of time used in economics are the short run and the long run. The short run refers to a period of time too brief to permit a firm to alter its plant capacity, yet long enough to permit a change in the production level at which the plant's fixed capacity is being utilized. In the short run, output can be varied by applying greater or lesser

locations differing only in that it was designed assuming each subscriber makes additional calls.⁸³ For the reasons previously cited, the Commission should not interpret the “additional cost” standard in this manner. Rather, “additional cost” should be computed for the total increment of a service provided. The same general principles apply in answer to the Commission questions of “[h]ow should we determine what costs are ‘incremental’?”⁸⁴ and “. . . are there any switching costs that would be considered incremental?”⁸⁵ Once again, the costs attributable to the total increment of a service provided should be used.⁸⁶

In conclusion, the Rural Alliance asserts that the use of embedded costs to determine the average incremental cost, with an allocation of joint and common cost, is consistent with the additional cost standard and with prior Commission findings. Use of embedded cost inputs, as opposed to forward-looking cost inputs, would be less burdensome for rural companies and thus would be administratively efficient. Embedded costs are also consistent with both the additional cost standard and the economic principles discussed above.

F. Intercarrier Compensation Rates Should Be Cost-Based, and Should Not Be Set at Target Rates.

amounts of labor, materials and other plant resources. The long run refers to a period of time sufficient to allow a firm to change the quantity of *all* resources used, including plant capacity.

⁸³ See *F NPRM* at ¶ 72.

⁸⁴ *Ibid.*

⁸⁵ *Ibid.*

⁸⁶ The incremental cost of switching for purposes of terminating calls consists of the total incremental cost of the traffic-sensitive portion of switching, which will be described in greater detail in a later section.

The Commission seeks comment on whether target rates should be established for rate-of-return LECs' access charges, and if so, what is the appropriate level of such rates.⁸⁷ Rather than setting target rates that do not reflect a particular LEC's cost, the Rural Alliance believes that intercarrier compensation rates, including access rates, should be set on the basis of each LEC's average incremental embedded costs, plus a reasonable allocation of joint and common costs.

The Commission previously examined the establishment of target rates for rate-of-return LECs' access charges when it considered the Multi-Association Group ("MAG") Plan to reform interstate access charges. The MAG Plan prescribed a single, target rate of 1.6 cents for rate-of-return LECs.⁸⁸ The Commission rejected this proposal on two counts.⁸⁹

First, the Commission observed that the target rate was inadequately supported by cost data:

No party has attempted to make a cost-based showing to support this proposal. Our examination of the record indicates that many rate-of-return carriers have traffic sensitive costs considerably higher than 1.6 cents per minute. Indeed, the comments filed in the above-captioned proceedings indicate a wide variation in cost patterns, density, and other operational characteristics among rate-of-return carriers.⁹⁰

No information has been introduced in this docket indicating that any of the prescribed intercarrier compensation rates included in proposals are cost-based, especially for rate-

⁸⁷ See *FNPRM* at ¶ 112.

⁸⁸ See *MAG Order* at ¶ 82.

⁸⁹ *Id.* at ¶¶ 83-84.

⁹⁰ *Id.* at ¶ 83.

of-return carriers. A prescribed intercarrier compensation rate less than 1.6 cents per minute will not result in proper pricing signals being sent to network users, for at least some rate-of-return LECs, given that many rate-of-return LECs have traffic-sensitive access costs higher than 1.6 cents per minute.

Second, prescribing a single access rate would not “foster the development of efficient competition in the exchange access market.”⁹¹ According to the Commission:

Rates that reflect an individual carrier’s cost of service provide the proper signals to permit a potential entrant to decide whether to enter a particular market. As [the National Association of State Utility Consumer Advocates (“NASUCA”)] observes, if a target rate were set too low, a barrier to competitive entry would be created. This is particularly so for carriers seeking to provide transport services alone as a means of entering a market.⁹²

Because a prescribed rate for intercarrier compensation cannot be cost-based for all LECs, such a rate will frequently send incorrect signals to users regarding the costs of using a particular network. As the Commission indicated, incorrect pricing signals, particularly if prices are set too low, result in a barrier to competitive entry. Given that one of the Commission’s stated goals is to promote development of efficient competition through intercarrier compensation reform, prescribing an access rate not based on cost would run counter to one of the Commission’s stated goals for this proceeding.

The Commission also seeks comment on whether the \$0.0095 rate adopted in the Coalition for Affordable Local and Long Distance Service (“*CALLS*”) Order might be an

⁹¹ *Id.* at ¶ 84.

⁹² *Ibid.*

appropriate rate, either as a transitional rate or as an end point.⁹³ The *CALLS* rate of \$0.0095 should not be applied to RLECs as it does not reflect the costs of high-cost companies. The arbitrarily selected *CALLS* rate for price cap carriers was \$0.0055 per minute for Regional Bell Operating Companies (“RBOCs”) and \$0.0095 per minute for non-RBOCs. Those non-RBOCs, that *voluntarily* selected price cap regulation, had unit costs that were decreasing faster than the price-cap indices. Either cost decreases or demand increases enabled these companies to make money under price cap regulation. Such cost characteristics are not representative of the high-cost, rural industry.

G. Rates Should Be Structured to Recognize the Traffic-Sensitive Nature of Network Elements.

In the event the current TELRIC methodology for pricing reciprocal compensation is retained, the Commission asks whether it should more precisely define what costs are traffic-sensitive, and thus recoverable through reciprocal compensation, and what costs are non-traffic-sensitive, and not recoverable through reciprocal compensation.⁹⁴ As a general principle, shared network resources are often traffic-sensitive, as increased usage usually requires installation of additional network resources to meet the demand. Such is the case for shared network resources such as switched transport and the majority of switching costs.

The Commission seeks comment on the traffic-sensitive nature of switching. Specifically, is switching cost primarily a function of the number of subscribers, not the

⁹³ See *FNPRM* at ¶ 72.

⁹⁴ *Id.* at ¶ 66.

number of calls or minutes of use (“MOU”).⁹⁵ The Commission observes that a number of parties to the TELRIC proceeding argued that the “. . . majority of switching costs do not vary with minutes of use (MOU) and that switching should be offered on a flat-rated basis rather than a per-minute basis.”⁹⁶ The Commission notes that a number of State commissions have also found end-office switching costs to not be traffic sensitive.⁹⁷ In making these observations, the Rural Alliance believes that both sides were not adequately represented. There was also evidence put forth in the pending TELRIC rulemaking that switching costs vary with minutes. Furthermore, some State commissions have found switching costs to be traffic sensitive.

Parties who attempt to justify the non-traffic sensitive nature of switching often use vendor contracts to support their claim.⁹⁸ These parties assert that LECs do not incur switching costs on a per-minute basis because vendor contracts establish per-line prices, rather than per-minute prices. Such logic is flawed because switching prices include an implicit assumption of usage per line; thus lines are simply a proxy for usage.

While there may be no separately stated price for usage in switch contracts, the equivalent line calculation is based on the type of termination and on anticipated usage. BellSouth gives the following example in its TELRIC Reply Comments:

For example, some equipment contracts have a line multiplier so that as usage increases, the line multiplier increases. Even though the vendor price may be stated in terms of lines, the number of lines to which the

⁹⁵ *Id.* at ¶ 67.

⁹⁶ *Ibid.*

⁹⁷ *Ibid.*

⁹⁸ *See FNPRM* at footnote 234.

price is applied is determined subsequent to the application of the line multiplier.⁹⁹

Furthermore, MCI, a party that argued that switches are not traffic-sensitive because vendor contracts for switches are stated in terms of lines instead of usage, has admitted in its TELRIC comments that pricing in this manner is driven by competitive concerns, not by cost causation.

. . . there is also evidence that the greatly simplified price structure found in the switch vendor contracts is a result of the increased level of competition between switch vendors. In order for switch vendors to demonstrate their relative competitiveness, they have an incentive to provide their clients (the ILECs and others) with a relatively simple “apples-to-apples” price comparison. It is easy to see how, in the face of competitive pressures, the previously complex pricing schemes would over time be reduced to a simple per-line price comparisons.¹⁰⁰

Parties attempting to justify that switching costs are not traffic sensitive also argue that switches generally have substantial excess capacity, and incorrectly draw the conclusion that increases in usage do not increase switching costs.¹⁰¹ The dictionary defines capacity as “the ability to contain, receive, or accommodate,” and “the maximum amount or number that can be contained.”¹⁰² If switching costs were not sensitive to usage, then a discussion of switch capacity would be unnecessary and irrelevant.¹⁰³

⁹⁹ See *In the Matter of Review of the Commission’s Rules Regarding the Pricing of Unbundled Network Elements and the Resale of Service by Incumbent Local Exchange Carriers*, WC Docket No. 03-173, Reply Comments of BellSouth (“*BellSouth TELRIC Reply Comments*”) (filed Jan. 30, 2004) at p. 69.

¹⁰⁰ See *In the Matter of Review of the Commission’s Rules Regarding the Pricing of Unbundled Network Elements and the Resale of Service by Incumbent Local Exchange Carriers*, WC Docket No. 03-173, Comments of MCI (filed Dec. 16, 2003) at p. 29, footnote 16, emphasis added.

¹⁰¹ See *ICC NPRM* at footnote 234.

¹⁰² Merriam-Webster, Dictionary, Home and Office Edition (1998).

¹⁰³ The Commission also asks if capacity constraints become obsolete as carrier migrate to Internet-protocol switching. See *FNPRM* at ¶ 68. Routers are sized based on offered load, and thus Internet-protocol switching is still based on capacity, specifically the ability to process the offered load.

Moreover, provisions in the Intercarrier Compensation Forum (“ICF”) plan to limit tandem exhaust would be unnecessary if switching costs are not sensitive to usage.¹⁰⁴ In addition, the ICF plan explicitly acknowledges the per-minute costs incurred by circuit-switched networks in its prescriptions for tandem transit service prices.¹⁰⁵

The majority of switch costs are usage-based. In fact, the only non traffic-sensitive component of a switch is a line termination port.¹⁰⁶ BellSouth indicates that at least two-thirds of the investment of a typical switch is usage sensitive. This conclusion is consistent with a study performed to establish switching rates for a transport and termination agreement approved by the Nebraska Public Service Commission (“NPSC”), which found 70 percent of switch cost to be traffic sensitive.¹⁰⁷ Consequently, the NPSC ordered that the ILEC in the arbitration case be paid compensation for switching on a minute-of-use basis.¹⁰⁸

Switches are engineered on a usage-sensitive basis.¹⁰⁹ For all switches, the processor and matrix are designed to meet the busy-hour load estimates. These busy-hour estimates consider toll usage, local phone usage and extended area service usage, as

¹⁰⁴ See *In the Matter of Developing a Unified Intercarrier Compensation Regime*, CC Docket No. 01-92, Appendices of the Ex Parte Brief of the Intercarrier Compensation Forum in Support of the Intercarrier Compensation and Universal Service Reform Plan Legal Brief (“*ICF Plan*”) (filed Oct. 5, 2004) at p. 30.

¹⁰⁵ See *ICF Plan* at pp. 28-29.

¹⁰⁶ See *BellSouth TELRIC Reply Comments* at p. 71.

¹⁰⁷ See *In the Matter of the Petition of Great Plains Communications, Inc. for Arbitration to Resolve Issues Relating to an Interconnection Agreement with WWC License, L.L.C.*, Nebraska Public Service Commission Application No. C-2872, Interconnection Agreement Approved as Modified, (“*Great Plains Arbitration Decision*”) (decided September 23, 2003) at ¶ 39.

¹⁰⁸ *Id.* at ¶ 43.

¹⁰⁹ See *BellSouth TELRIC Reply Comments* at p. 70.

well as regulatory service standards.¹¹⁰ The larger the load, the bigger the processor and matrix required, hence the higher the cost. BellSouth notes that in addition to the traffic sensitivity of the switch matrix, the links from line terminations to the switch matrix and most other components of the switch are traffic sensitive.¹¹¹ Not only are the processor and matrix of a switch traffic sensitive, but trunk terminations are also traffic sensitive because the total quantity of trunk terminations is based on the amount of inter-switch traffic.¹¹²

¹¹⁰ See *Great Plains Arbitration Decision* at ¶ 39.

¹¹¹ *Ibid.*

¹¹² See *BellSouth TELRIC Reply Comments* at p. 71.

The Commission also asks if such costs should be recovered on a per-minute or flat-rated capacity basis, once costs are identified as traffic-sensitive.¹¹³ While it may appear reasonable that end-office switching costs could properly be recovered from carriers on either a flat-rated capacity basis or on a usage basis, in fact, the Commission has already specified how traffic-sensitive costs are to be recovered in rates:

[f]or the purposes of setting rates under section 252(d)(2), only that portion of the forward-looking, economic cost of end-office switching that is recovered on a usage-sensitive basis constitutes an “additional cost” to be recovered through termination charges.¹¹⁴

Thus, under current rules only those charges that are recovered on a usage-sensitive basis can be included in a reciprocal compensation rate in order to meet the additional cost standard.

H. Transport Rates Should Be Structured to Recognize Traffic-Sensitivity and Distance-Sensitivity.

Inter-carrier compensation rates should be structured to recognize that switched transport costs are both traffic-sensitive and distance-sensitive. Switched transport costs are traffic-sensitive, because the number of switched transport trunks must necessarily increase as the amount of switched traffic at the peak-load period increases. If trunks were not added as switched traffic increased, blockage could occur during the peak-load period. Switched transport costs are also distance sensitive. With the exception of terminal equipment, all costs to install switched transport are incurred on a per-mile basis; therefore, the more miles of switched transport, the greater the cost.

¹¹³ See *FNPRM* at ¶ 70.

¹¹⁴ See *Local Competition Order* at ¶ 1057.

Because switched transport rates are both traffic sensitive and distance sensitive, a target per minute rate for transport, such as the \$0.0095 per minute suggested in the ICF plan, will not appropriately compensate LECs for the distance sensitivity of their networks. Under the ICF plan, the \$.0095 per minute rate was only meant to compensate a LEC for the portion of its network between the meet point and the LEC's edge. The remaining portion of the network, between the edge and the rest of the LEC's end offices, is subject to bill and keep. For RLECs, the distances involved can be substantial — even hundreds of miles. A target per minute rate for transport that does not provide compensation for intracompany transport will discriminate in favor of urban LECs relative to RLECs with long transport mileages. Furthermore, a per-minute rate independent of distance will not send appropriate price signals to network users. Such a pricing structure would make it appear to users that the costs of transport on all networks are the same, which is clearly not the case. The Rural Alliance therefore recommends that switched transport rates be structured to recognize that this service is both traffic sensitive and distance sensitive.¹¹⁵

I. Rate Structure Issues Should Be Addressed in a Further Notice of Proposed Rulemaking.

The Rural Alliance respectfully suggests that the Commission can resolve many of the arbitrage problems plaguing the industry simply by clarifying its current rules and

¹¹⁵ The Rural Alliance also believes that any target rate is inappropriate because, as discussed in a previous section, it would not reflect the cost variation that occurs among carriers.

unifying rate levels.¹¹⁶ Major structure changes, with possible unanticipated consequences, deserve additional consideration. As such, the Rural Alliance believes that rate structure issues, such as those raised in the *FNPRM*,¹¹⁷ should be deferred to a future proceeding. Specifically, a Further Notice should be initiated to examine capacity-based intercarrier compensation charges for switched services and session-based charges for the Digital Subscriber Line (“DSL”) rate structure. Since rate structures will have significant implications for intrastate compensation, the Commission should also refer rate structure issues to a Joint Board.

The Commission currently also has rate structure issues pending before it in the TELRIC proceeding.¹¹⁸ While the Rural Alliance is not suggesting that intercarrier compensation rates be structured in exactly the same manner as UNE rates, it does believe that instead of developing rate structures in a piecemeal fashion in different proceedings at different times, it would be prudent to examine rate structure issues in a more comprehensive fashion.

J. The Rural Alliance Examines the Efficacy of the Major Plans.

1. The ICF Plan Will Not Allocate Resources in an Optimal Manner.

The bill-and-keep regime proposed by the ICF represents a radical departure from current intercarrier compensation. The plan eliminates the access charge regime and reduces reciprocal compensation rates to zero. While the Rural Alliance agrees that

¹¹⁶ Presumably the harmful effects of per minute charges that the Commission refers to in ¶ 23, n. 67 of the *FNPRM* relate to traffic bound to an Internet Service Provider (“ISP”). Such problems will be resolved if the Commission adopts the Rural Alliance proposal on ISP-bound traffic in Section VI of these comments.

¹¹⁷ See *FNPRM* at ¶ 70.

unification of intercarrier compensation rate levels is needed, rate unification does not imply that the distinction between exchange access and reciprocal compensation should be eliminated.

Bill and keep may be economically efficient in certain voluntary situations when the following criteria are met: (a) The carriers have similar cost structures; (b) Traffic is balanced; and (c) The underlying service is conducive to a bill-and-keep arrangement. A service is conducive to a bill-and-keep arrangement when the service represents a mutual exchange of like traffic, not when one entity unilaterally uses the facilities of a wholesale provider. By eliminating exchange access, the ICF ignores the vital role played by a wholesale service provider. Under the plan, the entity that receives revenue for a call does not have to pay for its network use, because originating access is eliminated and transport is only paid for facilities to the edge of the terminating LEC's network.

If prices of origination and termination do not reflect actual cost, usage will increase uneconomically. If the ICF plan were adopted, competitive pressures would force individual IXC's to set retail prices to recover their internal costs, as opposed to actual network costs plus internal costs. Thus, long distance consumers will no longer receive true cost-based pricing signals. The only way network resources will be allocated in an optimal manner is if prices reflect the actual cost of providing the network resources. Since resources would not be allocated optimally, the ICF's bill-and-keep scheme conflicts with the Commission's goal of promoting economic efficiency. Moreover, the cost of building, maintaining and provisioning a local network is obviously not zero. Therefore, a compensation rate of zero for use of a network with non-zero cost

¹¹⁸ See *TELRIC NPRM*.

characteristics is also at odds with NARUC's principle of appropriate network cost recovery.¹¹⁹

Increased levels of long distance calling will require increased capacity in the local networks that originate and terminate such traffic. To meet such demand increases, LECs must make plant investments, particularly in interoffice transport and switch trunking, and they would have no economic incentive to make the needed investments. Unlike the ICF plan sponsors, both the Rural Alliance and NARUC¹²⁰ maintain that traffic volume must be acknowledged in the rate structure.

2. *The ICF Plan Discriminates Among Different Network Classifications.*

The ICF approach is philosophically inconsistent with the goal of a unified regime because the approach treats entities differently based on their classification. Such discrimination should not be the basis for any intercarrier compensation reform. While the Commission has previously allowed exceptions to its general rules, such exceptions were based on fact, not arbitrary distinctions. For example, RLECs are allowed to receive universal service funding based on embedded costs rather than forward-looking cost in part because cost models don't adequately reflect rural costs.¹²¹ Such exceptions should be allowed, but they should not be unduly discriminatory.

The ICF plan contains a general rule that each carrier must transport outbound PSTN interconnection traffic to the edge designated by the interconnecting carrier. The

¹¹⁹ See *NARUC Principles* III.B: "[i]ntercarrier compensation should be designed to recover an appropriate portion of the requested carrier's applicable network costs."

¹²⁰ See *NARUC Principles* III.F: "Volume of use should be considered when setting intercarrier compensation rates. Available capacity may be used as a surrogate for volume of use."

¹²¹ See *RTF Order* at ¶¶ 4-11.

general rule has two exceptions based on the carriers' categorization. One exception, frequently termed the "rural carve out," specifies that interconnecting carriers must establish an edge on the rural company's network. This so-called "carve out" is simply a restatement of current law, which requires carriers to interconnect on the ILEC's network. The Act and the Commission's rules only require that an ILEC establish an interconnection point with a requesting carrier "at any technically feasible point *within the carrier's network*." The other exception refers to an interconnection situation between a hierarchical carrier and a non-hierarchical carrier.¹²² The ICF plan requires the non-hierarchical carrier to pay for interconnection transport between the carriers' edges *in both directions* — a result that clearly discriminates in favor of hierarchical carriers.

Another form of discrimination in the ICF plan occurs for Covered Rural Telecommunications Carriers ("CRTCs")¹²³ utilizing Centralized Equal Access ("CEA"):

If an Access Tandem is the source of equal access functionality, then the CRTC must designate that Access Tandem as its Edge for carriers that require equal access for interconnection, in which case the CRTC will be financially responsible for all transport costs in both directions on its side of the Access Tandem.¹²⁴

¹²² "A Hierarchical Network is one (other than a Rural Network, as defined below) in which End Offices subtend an Access Tandem owned by the owner of such End Offices. As used in this Plan, the term 'Hierarchical Carrier' shall mean a carrier to the extent it is engaged in the operation of a Hierarchical Network. A Rural Network is one operated by a Covered Rural Telephone Company ("CRTC") as defined below. A Non-Hierarchical Network is one that is neither a Hierarchical Network nor a Rural Network. As used in this Plan, the term 'Non-Hierarchical Carrier' shall mean a carrier to the extent it is engaged in the operation of a Non-Hierarchical Network." *See ICF Plan* at pp. 9-10.

¹²³ "A 'Covered Rural Telephone Company' is an ILEC that, as of July 1, 2005 and excluding those exchanges that are subject to the provision for acquired exchanges, (a) meets the definition of a 'Rural Telephone Company' ... or (b) qualifies as a two percent carrier under the criteria established in section 251(f)(2). *See ICF Plan* at p. 19.

¹²⁴ *Ibid.*

Following this rule, when a CRTC connects indirectly with an IXC (a non-hierarchical carrier) through an access tandem with equal access functionality, the CRTC is responsible for *all* transport on its side of the CEA tandem. On the other hand, when a CRTC connects indirectly with an IXC through an access tandem that is *not* the source of equal access functionality, the IXC's financial obligations include transporting terminating traffic to the CRTC's edge and transporting originating traffic from a point within the CRTC's serving area to the transit provider.¹²⁵

The ICF plan also proposes that CEA operators will not be allowed to charge IXCs for transiting, even though CEA operators provide a service identical to the RBOCs' transiting service. A CEA tandem provider performs the same functions as a transiting provider and should not be discriminated against as proposed under the ICF plan. By disadvantaging LECs that use a CEA tandem, the ICF creates unfair and unwarranted incentives to use RBOC transiting.

Such disparate treatment means that CRTCs utilizing CEA arrangements are clearly discriminated against. The IXC's retail traffic utilizes the CEA tandem, yet the IXC contributes minimally to the cost of transporting and switching such traffic. In contrast, when a CRTC does not use a CEA tandem, the CRTC receives terminating transport. The CRTC's choice to utilize CEA technology should have no bearing whatsoever on the financial responsibility for transport. Moreover, IXCs cannot be billed for CEA transiting services under the ICF plan, yet the same services offered by RBOCs can be billed. Such instances of discrimination in an intercarrier regime would invite

¹²⁵ *Id.* at p. 27.

legal challenges, would create arbitrage opportunities and contradict NARUC's principle that all entities using a service should be charged the same amount.¹²⁶

3. *The ICF Plan Violates Section 252(d)(2) of the Act.*

The ICF plan *forbids* a carrier from “mutual and reciprocal” recovery of its “costs associated with the transport and termination on [its] network facilities of calls that originate on the network facilities of [another] carrier.”¹²⁷ Such a mandatory bill-and-keep regime would violate section 252(d)(2) of the Act, which was included to allow local carriers to recover the “additional costs” associated with switching and transport caused by the actions of another local carrier's customer.

The ICF argues that the cost “recovery” to which section 252(d)(2)(A) refers can be interpreted to mean “recovery of those costs from *its own end users*,” consistent with a bill-and-keep regime.¹²⁸ In fact, the cost recovery that section 252(d)(2)(A)(i) addresses is “mutual and reciprocal recovery by *each carrier* of costs associated with the transport and termination on each carrier's network facilities of calls that originate on the network facilities of the other carrier.”¹²⁹ The Act thus specifically distinguishes between recovery of costs from end users and recovery of costs from carriers. The ICF attempts

¹²⁶ See *NARUC Principles* III.C.: “A carrier that provides a particular service or function should charge the same amount to all Covered Entities to whom the service or function is being provided. Charges should not discriminate among carriers based on:

1. the classification of the requesting carrier;
2. the classification of the requesting carrier's customers;
3. the location of the requesting carrier's customer;
4. the geographic location of any of the end-users who are parties to the communication; or,
5. the architecture or protocols of the requested carrier's network or equipment.”

¹²⁷ See *ICF Brief* at p. 38.

¹²⁸ *Id.* at p. 39.

¹²⁹ 47 U.S.C. 252(d)(2)(A)(i), emphasis added.

to distort these distinctions in order to support a plan that would force end users to pay costs Congress intended to be paid by carriers.

While the ICF claims section 252(d)(2)(B)(i) expressly authorizes bill-and-keep arrangements, no language in section 252(d)(2) conveys any regulatory authority to the Commission to impose a mandatory bill-and-keep regime.¹³⁰ Section 252(d)(2)(B)(ii) even explicitly prohibits the Commission from using its section 252(d) authority to engage in a rate regulation proceeding to find that the additional cost of transporting or terminating calls is zero. The ICF brief argues incorrectly that legislation that *forbids a prohibition* of certain acts authorizes regulation to make those acts *mandatory*.¹³¹ Such an interpretation cannot stand given that Congress specifically added a reference in the Act to “bill-and-keep arrangements” as examples of “arrangements that *waive* mutual recovery”¹³² in an effort to highlight that bill-and-keep arrangements are inconsistent with mutual cost recovery.

4. *The ICF Plan Creates New Arbitrage Opportunities.*

The ICF plan is presumably designed to eliminate arbitrage by correcting the industry’s disparate prices, but the plan will end up creating several new forms of arbitrage.¹³³ First, customers that generate large amounts of originating long distance

¹³⁰ See *ICF Brief* at p. 39.

¹³¹ 47 U.S.C. 252(d)(2)(B), emphasis added, which reads, in part “This paragraph shall *not* be construed ... to *preclude* arrangements....”; emphasis added.

¹³² In a bizarre *non sequitur*, the ICF brief makes the claim that “[b]ill and keep, as structured in the ICF Plan, entitles carriers to the ‘mutual recovery of costs’ by permitting them to recover those costs through end-user charges and, where necessary, universal service” *immediately following* a quotation from 47 U.S.C. 252(d)(2)(B)(i). See *ICF Brief* at p. 39.

¹³³ Arbitrage occurs when two perfectly substitutable products are simultaneously bought and sold at two different prices in two different markets.

traffic will substitute the special access services purchased currently with free, or nearly free, switched access. The replacement of one product with another priced at a different rate represents arbitrage. Second, as the Commission notes in its Central Office Bill And Keep (“COBAK”) paper, an organization might even create its own IXC to avoid local service charges, thus arbitraging local and switched access service.¹³⁴

In addition to arbitrage, unintended consequences will likely result from bill and keep. Customers who receive no pricing signals regarding consumption of a scarce resource will tend to overuse that resource. Specifically, a customer will have no motivation to “hang up” a call, because the call is free, or nearly so. Expensive switch resources will be used in a manner more aptly suited to special access service. In addition, an Internet Service Provider (“ISP”) with multiple modem pools established for local dial-up Internet calls would be motivated to consolidate these pools. At the extreme, an ISP might even create a single national modem pool. While one might argue that such a scenario would be efficient and benefit customers, the impact on the telephone network would be devastating as switching and transport resources are needlessly consumed nationwide and additional costs are imposed on wholesale network providers.

The ICF plan would merely replace one set of arbitrage opportunities with another, not reduce or minimize such opportunities. A bill-and-keep regime that encourages end users to masquerade as carriers or to substitute special access with free switched access does little to eliminate the arbitrage opportunities present in current intercarrier compensation arrangements. By failing to resolve arbitrage, the ICF plan

¹³⁴ Patrick DeGraba, “Bill and Keep at the Central Office As the Efficient Interconnection Regime,” FCC Office of Plans and Policy - Working Paper No. 33, (Dec 2000) at ¶ 88.

does not comply with NARUC's principle that compensation plans should minimize arbitrage opportunities and be resistant to gaming.¹³⁵

5. *The ICF Plan Provides a Cost Advantage for Interexchange Carriers.*

The ICF Plan requires LECs to provide IXC's access to the LEC's wholesale networks at no charge. Such a scheme unduly favors IXCs that depend on LECs for access to their customers because these IXCs have no local facilities of their own. The cost shift inherent in the ICF plan removes costs from IXCs without local facilities and adds costs to entities operating local networks. IXCs thus have a competitive advantage relative to other long-distance providers, such as Commercial Mobile Radio Service ("CMRS") or facilities-based Voice over Internet Protocol ("VoIP") providers, which operate their own local network.

6. *The ICF Plan Fails to Recognize the Cost of Long-Transport Routes in Rural Markets.*

Under the ICF plan, a CRTC may assess a Terminating Transport Charge, at a rate of \$.0095 per minute, to carriers (other than fellow CRTCs) for the delivery of terminating traffic from any point within the CRTC's territory to its designated edge.¹³⁶ A target rate, as proposed by the ICF, fails to conform to the NARUC principle requiring a new intercarrier compensation system to recognize that some rural areas have much higher costs than others do.¹³⁷ One LEC's costs are not necessarily comparable to another's simply because both qualify as being rural. Differences in geography,

¹³⁵ See NARUC Principles III. A.: "The compensation plan should minimize arbitrage opportunities and be resistant to gaming."

¹³⁶ See ICF Plan at pp. 37-38.

¹³⁷ See NARUC Principles VII. B.: "A new intercarrier compensation system should recognize that areas served by some rural local exchange carriers are significantly more difficult to serve and have much higher costs than other areas."

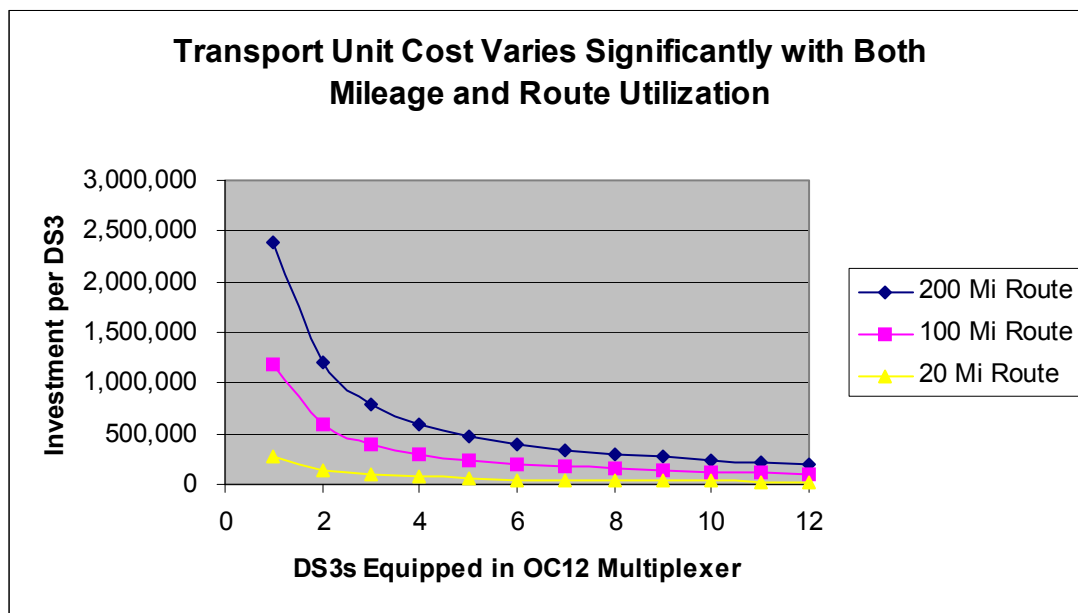
topography, distance and density all affect rural costs. For example, there is a significant cost difference between a RLEC that serves one 5,000 line exchange and a RLEC serving 5,000 lines in 20 exchanges spread over hundreds of square miles.

The Terminating Transport Charge is also inadequate because it only provides recovery for traffic from the network meet point (most often the study area boundary) to the “edge” designated by the CRTC.¹³⁸ According to the ICF, “[A] CRTC must establish an Edge within each Contiguous Portion of the CRTC’s Study Area within a Local Access and Transport Area (“LATA”) (or, in a non-LATA State, local calling area.)”¹³⁹ By requiring one edge per study area, the ICF has created a situation where a significant portion of transport remains uncompensated. An RLEC may have long transport distances with very low traffic volumes occurring behind the edge. Such distances may be much greater than the distance from the meet point to the edge. Under the ICF plan, the RLEC would be forced to carry traffic at no cost from the edge to the central office serving the customer. The ICF plan supposedly allows transport recovery from the LEC’s end users, but the transport costs in very sparsely populated areas will be much too high to recover from the end users.

The proposed Terminating Transport Charge also fails to recognize the cost drivers associated with rural transport routes. Transport costs are a function of both trunk size and transport distance, as shown in Figure 1.

¹³⁸ See *ICF Plan* at p. 37.

¹³⁹ *Id.* at p. 19.



* Costs are based on the cost of Alcatel equipment in a small rural company.

Fig. 1 – Unit Costs are Higher for Longer Distances and Lower Traffic Volume

As illustrated in Figure 1, companies faced with long transport distances and low traffic volumes (as evidenced by low numbers of DS3) face much higher costs than companies with short transport distances and high volumes. Figure 1 demonstrates that transport costs are a strong function of both distance and traffic load. The costs are significantly higher when transport involves both long distances and low volumes of traffic. An approach, such as the ICF plan, that does not represent these cost dependencies is flawed. If RLECs operating in low density, geographically challenging markets are not adequately compensated, rural end users will see an unacceptable increase in costs or RLECs will be economically incapable of continuing to provide service.

7. *Western Wireless' Proposal Has the Same Economic Problems as the ICF's Plan.*

Western Wireless, like the ICF, recommends a bill-and-keep solution for intercarrier compensation. Although Western Wireless proposes an implementation time frame that is longer for RLECs than for larger companies,¹⁴⁰ the Rural Alliance reaffirms the same objections to all bill-and-keep proposals, regardless of the implementation speed or the mechanics employed in reducing rates to zero.

8. *CBICC's Intercarrier Compensation Plan Results in Rates Too Low for Rural Areas.*

The Cost-Based Intercarrier Compensation Coalition ("CBICC") believes that "the State established TELRIC rate for local switching, transport and termination is the correct rate" for all forms of intercarrier compensation.¹⁴¹ The Rural Alliance, however, maintains that the TELRIC rate alone does not adequately cover an RLEC's cost of providing switching, transport, and termination services. Reduction of rates to TELRIC levels would result in a substantial revenue loss for RLECs, in part because such an approach does not include a reasonable allocation of joint and common costs. To base rates on TELRIC alone, without a reasonable allocation of joint and common costs, would be inconsistent with the Commission's current approach to defining the additional cost standard, which includes an allocation of joint and common costs.

Despite a disagreement about rate setting, the Rural Alliance agrees with several other principles enumerated in the CBICC proposal. The Rural Alliance joins with

¹⁴⁰ "Over a 4 year period, the maximum level of per-minute intercarrier compensation rates subject to interconnection agreements declines to zero (bill-and-keep). For the smallest rural ILECs (those with fewer than 30,000 lines in a state and fewer than 100,000 nationwide), these reductions would proceed on a slower time frame (e.g., six years instead of four)." See *Western Wireless Plan* at p. 2

¹⁴¹ *In the Matter of Developing a Unified Intercarrier Compensation Regime*, CC Docket No. 01-92, Ex Parte Brief of the Cost-Based Intercarrier Compensation Coalition, ("*CBICC Plan*") (filed Sept. 2, 2004) at p. 1.

CBICC in rejecting any proposal that would impose a mandatory bill-and-keep regime. Although the Rural Alliance does not agree with the rate proposal, it does agree with CBICC's general principle of adopting a unified, cost-based rate, including a per-minute switching rate. In addition, the Rural Alliance concurs with CBICC's premise that intercarrier compensation must reflect current retail and wholesale relationships. For traffic involving three or more carriers, CBICC proposes that "the carrier with the *retail relationship with the originating caller* pays all other carriers whose networks are used to complete a call."¹⁴² CBICC is thereby endorsing the concept of Retail Service Provider Pays, which will be discussed in Section IV.

9. *NASUCA Supports a Non-zero Rate and Adheres to the "Retail Service Provider Pays" Concept.*

The Rural Alliance agrees that the concept of carrier-to-carrier cost causation must be reflected in any intercarrier compensation regime and joins with NASUCA in rejecting proposals that mandate a zero intercarrier compensation rate. NASUCA believes that "any plan for ICC reform must recognize that a carrier that originates, transits or terminates traffic on the network of another carrier imposes costs on that carrier. As a result, the cost of intercarrier compensation cannot be zero."¹⁴³ On the other hand, the Rural Alliance disagrees with NASUCA's assertion that a rate of \$.0095 per minute would be compensatory for RLECs.¹⁴⁴ Such a rate level is much lower than

¹⁴² *CBICC Plan* at p. 2, emphasis added.

¹⁴³ *In the Matter of Developing a Unified Intercarrier Compensation Regime*, CC Docket No. 01-92, National Association of State Utility Consumer Advocates Intercarrier Compensation Proposal, ("*NASUCA Proposal*") (filed Dec. 14, 2004) at p. 1.

¹⁴⁴ *Id.* at p. 1.

current interstate or intrastate access rates, as well as lower than many arbitrated reciprocal compensation rates.

NASUCA also recognizes the significance of existing wholesale and retail relationships and proposes that these relationships remain unchanged.¹⁴⁵ The Rural Alliance agrees that existing wholesale relationships between IXC's and LEC's, as well as the retail relationships between an IXC and an end-user consumer should not be undermined or eliminated through adoption of an intercarrier compensation plan.

¹⁴⁵ *Ibid.*

III. ANY INTERCARRIER COMPENSATION MECHANISM ADOPTED BY FEDERAL AND STATE REGULATORS MUST BE STRUCTURED TO PRESERVE UNIVERSAL SERVICE.

As the Commission's *FNPRM* properly recognizes, preservation of universal service is a mandate that must be fulfilled when considering any intercarrier compensation regime.¹⁴⁶ Numerous principles contained in the Act require that universal service be ensured, including:

Section 254(b)(1) QUALITY AND RATES. – Quality services should be available at just, reasonable, and affordable rates.

Section 254(b)(2) ACCESS TO ADVANCED SERVICES. – Access to advanced telecommunications and information services should be provided in all regions of the Nation.¹⁴⁷

Section 254(b)(3) ACCESS IN RURAL AND HIGH COST AREAS. – Consumers in all regions of the Nation, including low-income consumers and those in rural, insular, and high cost areas, should have access to telecommunications and information services, including interexchange services and advanced telecommunications and information services, that are reasonably comparable to those services provided in urban areas and that are available at rates that are reasonably comparable to rates charged for similar services in urban areas.

Section 254(b)(5) SPECIFIC AND PREDICTABLE SUPPORT MECHANISMS. – There should be specific, predictable, and sufficient Federal and State mechanisms to preserve and advance universal service.

Section 254(b)(7) ADDITIONAL PRINCIPLES. – Such other principles as the Joint Board and the Commission determine are necessary and

¹⁴⁶ *FNPRM* at ¶ 32.

¹⁴⁷ President Bush has, in fact, made access to broadband services for all Americans by 2007 a cornerstone of his administration's economic policy. See *Remarks by the President on Innovation*, U.S. Department of Commerce, <http://www.whitehouse.gov/news/releases/2004/06/20040624-7.html>.

appropriate for the protection of the public interest, convenience, and necessity and are consistent with this Act.¹⁴⁸

This combination of principles is a powerful and important directive from the nation's lawmakers on universal service assurances for all Americans. The Rural Alliance believes these principles establish a template that demands a balance between intercarrier compensation reforms and the nation's universal service statutes. Several of NARUC's intercarrier compensation reform principles support the same conclusion – preservation of universal service.¹⁴⁹

A. Cost Recovery Should Continue to Consist of a “Three-Legged Stool” Among Revenue Sources.

Network cost recovery has long been represented by a “three-legged” stool consisting of local service revenues, intercarrier revenues, and universal service support. Consistent with this analogy, all “legs” must be strong and stable enough for the stool – in this case, network cost recovery – to remain balanced and viable. A loss or large

¹⁴⁸ The Joint Board on Universal Service and the Commission have adopted an additional universal service principle that requires that any universal service support also should be competitively neutral. *See In the Matter of Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Recommended Decision FCC 04J-1 (rel. Feb. 27, 2004) at ¶ 70 and First Report and Order, FCC 97-157 (rel. May 8, 1997) at ¶ 19.

¹⁴⁹ *See NARUC Principles*:

- VII. A. The transition to a new intercarrier compensation system should ensure continuity of existing services and prevent significant rate shock to end-users. Penetration rates for basic service should not be jeopardized.
- VII. B. A new intercarrier compensation system should recognize that areas served by some rural local exchange carriers are significantly more difficult to serve and have much higher costs than other areas.
- VI. C. To avoid creating harmful economic incentives to de-average toll rates by some interexchange carriers, the FCC should have authority to pool costs within its defined jurisdiction whenever intercarrier compensation rates are high in some areas.
- VII. C. Rural customers should continue to have rates comparable to those paid by urban customers. End-user basic local exchange rates should not be increased above just, reasonable, and affordable levels.
- VII. D. Any intercarrier compensation plan should be designed to minimize the cost impact on both federal and State universal service support programs.

reduction in any of these sources will cause the stool to wobble, if not outright collapse. To that end, the reductions in current intercarrier compensation revenues that are likely a result of this proceeding must be replaced by additional universal service support or other mechanisms to maintain the standards of affordability and comparability required by the above-cited principles in the Act.

1. *Inter-carrier Compensation Revenue Reductions Should Be Offset Through Other Mechanisms.*

In the *FNPRM*, the Commission asks a series of questions related to how cost recovery should occur if access revenues for either price cap or rate-of-return LECs are reduced.¹⁵⁰ The Commission specifically asks what is its legal obligation to provide alternative cost recovery mechanisms, as well as whether elimination of access charges would be confiscatory in the absence of such mechanisms.¹⁵¹

Assuring rate-of-return LECs the opportunity to recover an authorized rate of return on their interstate access services is a fundamental tenet of rate-of-return regulation and long-existing Commission rules.¹⁵² In addition, comparability standards limit the amount of increases that can be imposed on customers in the form of higher end-user charges or SLCs. If a rate-of-return company's SLCs are already at the caps and its local rates are reasonable, then it is only appropriate that the company recovers lost intercarrier compensation revenues from universal service support or other mechanisms. Revenue

¹⁵⁰ *FNPRM* at ¶¶ 99, 101, 108, 111, and 114.

¹⁵¹ *See FNPRM* at ¶ 99.

¹⁵² *See Re-prescribing the Authorized Rate of Return for Interstate Services of Local Exchange Carriers*, CC Docket No. 89-624, 5 FCC Rcd 7507. *See also* 47 C.F.R. § 65.

replacement will assure that the company has adequate revenues to recover its costs and meet its universal service obligations.

Through the reforms the Commission implements in this docket and other related dockets,¹⁵³ along with those decisions made by each State commission with responsibilities for its respective State, the Commission can inject stability into the market. For rate-of-return LECs serving much of this nation's rural, high-cost areas, such stability should optimally ensure that reforms are revenue neutral, costs are recovered in a cost-causative manner, and balance is maintained among revenue sources.

The Commission also solicits input on whether it is "legally obligated" to make any transition to a new compensation regime revenue neutral for affected carriers.¹⁵⁴ While a specific legal obligation may not exist to require revenue neutrality, the Commission should seek to minimize disruption by ensuring that LECs have the opportunity to recover their current revenues.¹⁵⁵ To do otherwise would cause further stress on the struggling telecommunications industry, which needs stability at this critical time to help stimulate the nation's economic recovery. In the absence of revenue stability, small and mid-size LECs will not be able to attract or sustain the financing needed for deployment and maintenance of plant.

¹⁵³ Related dockets that are currently open, and with which the Commission should also move forward to inject stability into the marketplace, include CC Docket No. 96-45, *In the Matter of Federal-State Joint Board on Universal Service*, and WC Docket No. 04-36, *In the Matter of IP-Enabled Services*.

¹⁵⁴ See *FNPRM* at ¶ 100.

¹⁵⁵ If revenue replacement were not done on a revenue-neutral basis, then presumably an earnings review would be incorporated into the determination of the amount of revenue replacement a company would receive. Most states already have mechanisms for handling earnings and many companies are under an alternative form of regulation, other than rate of return, at the state level. Since this proceeding addresses fundamental changes in all aspects of intercarrier compensation, adding earnings reviews necessarily increases the complexity of an already highly complex proceeding.

2. *Customer Impacts Are of Utmost Consideration in Reforming Inter-carrier Compensation.*

The Rural Alliance believes the Commission not only has an obligation to provide alternative cost recovery, but it must also recognize its own long-standing principle of recovering costs in the manner in which costs are caused.¹⁵⁶ As discussed in these Comments, switching and transport costs are traffic sensitive and thus properly included in the rates paid by carriers. In addition to recovering costs consistent with the manner in which costs are incurred, maintaining cost-causative rates will ensure end-user customers are not overburdened with excessive rate increases.

The Commission asks a series of questions regarding the impact on customers of replacing access charges with additional subscriber charges and/or universal service support.¹⁵⁷ With these questions, the Commission seemingly recognizes that customers will not necessarily benefit from inter-carrier compensation reductions. Indeed, the Commission also recognizes the distinct possibility that high-volume users will “reap most of the benefits” of a proposal to eliminate interstate access charges.¹⁵⁸ Aside from limiting drastic reductions in inter-carrier compensation, there is little that can be done to protect customers – particularly low-volume ones.

A long-standing objective of the Commission in its previous inter-carrier compensation proceedings has been to eliminate what it has categorized as “implicit

¹⁵⁶ See *In the Matter of Access Charge Reform*, CC Docket No. 96-262, *Price Cap Performance Review for Local Exchange Carriers*, CC Docket 94-1, *Transport Rate Structure and Pricing*, CC Docket No. 91-213, and *End User Common Line Charges*, CC Docket No. 95-272, First Report and Order, FCC 97-158 (rel. May 16, 1997) at ¶¶ 36-42; See also *MAG Order* at ¶ 17.

¹⁵⁷ See *FNPRM* at ¶ 106.

¹⁵⁸ *Ibid.*

subsidies” existing in rates.¹⁵⁹ The Commission, however, has never identified what constitutes “implicit subsidy” or distinguished “implicit subsidy” from other network costs recovered from rates. As a result of this omission, the *MAG Order* inappropriately resulted in subsidization of carriers who utilize RLECs’ transport facilities by wrongly converting some costs previously and properly recovered in the Transport Interconnection Charge into portable Interstate Common Line Support (“ICLS”).¹⁶⁰ The Rural Alliance respectfully urges the Commission to use caution as it implements this round of intercarrier compensation reform to ensure that this mistake is not repeated. The inappropriate shift of the remaining switching and transport costs related to intercarrier services into increased end-user rates will exacerbate the unresolved issues arising from the *MAG* proceeding. To do so would unfairly burden rural customers with higher rates, by including intercarrier costs in those rates. By removing costs properly recovered in intercarrier rates, the Commission would thus be creating a new implicit subsidy in violation of section 254(k).

3. *The Same SLC Cap Should Be Maintained for Price Cap and Rate-of-Return LECs.*

¹⁵⁹ See, generally, *CALLS Order* and *MAG Order*.

¹⁶⁰ See *In the Matter of Multi-Association Group (“MAG”) Plan for Regulation of Interstate Services for Non-price cap Incumbent Local Exchange Carriers and Interexchange Carriers*, CC Docket No. 00-256, *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, *Access Charge Reform for Incumbent Local Exchange Carriers Subject to Rate of Return Regulation*, CC Docket No. 98-77, and *Prescribing the Authorized Rate of Return for Interstate Services of Local Exchange Carriers*, CC Docket No. 98-166, Petition for Reconsideration of Plains Rural Independent Companies, (filed Dec. 31, 2001). The petition requests that the Commission reverse its decision to convert transport costs previously recovered from the TIC into the newly created ICLS. The Commission has not yet addressed issues raised in the petition. The Rural Alliance urges that the petition be granted as part of the proper establishment of cost-based rates in this proceeding, since elimination of the TIC created an anti-competitive advantage for companies that use rural ILECs’ interstate transport but do not pay for most of the cost of that transport.

The Commission seeks comment on whether SLC caps should remain the same for both price cap and rate-of-return ILECs.¹⁶¹ If one assumes that local rate benchmarks are ultimately implemented as described later in this filing, comparable rates between urban and rural customers cannot be maintained if the current SLC caps are increased without other actions. Current SLC levels vary widely between customers served by price cap and rate-of-return ILECs, with most rate-of-return carriers' SLCs having already reached the caps while price cap carriers' SLCs remain well below the caps.¹⁶² Therefore, any increase in SLC caps for all carriers would only result in an expansion of the existing disparity between customers of price cap and rate-of-return ILECs, thus running afoul of the universal service comparability standard. Plans that significantly increase SLC caps, such as the ICF plan, will only exacerbate the existing gap in SLC levels.¹⁶³

A more-constructive issue to consider is the extent to which price cap ILECs whose existing SLCs are below the caps should be permitted to increase SLCs to make up for reduced intercarrier compensation revenues. Given that many price cap ILECs' SLCs are well below the current caps,¹⁶⁴ the Commission should consider allowing price cap ILECs to increase SLCs to the current caps as a means of offsetting lost revenues.¹⁶⁵

¹⁶¹ See *FNPRM* at ¶¶ 101-102, and 108.

¹⁶² See *In the Matter of Developing a Unified Intercarrier Compensation Regime*, CC Docket No. 01-92, The Intercarrier Compensation Reform Plan of the Alliance for Rational Intercarrier Compensation, ("*ARIC Plan*") (filed Oct. 25, 2004) at pp. 25-26.

¹⁶³ The ICF plan proposes to raise SLC caps to \$10 plus inflation and later would allow SLC de-averaging and elimination of caps.

¹⁶⁴ See *ARIC Plan* at pp. 25-26.

¹⁶⁵ To the extent a price cap carrier is below the SLC caps, recovery of traffic-sensitive intercarrier compensation costs under the existing SLC caps is a component of the ARIC Fair Affordable

In addition to the significant revenue recovery opportunity that this measure would afford, permitting price cap ILECs' costs to be shifted into SLCs would also help achieve true end-user rate comparability among all customers.

The Commission also asks whether new revenue opportunities or cost reductions should be factored into cost recovery for price cap carriers.¹⁶⁶ Should companies experience significant cost reductions as a result of intercarrier compensation reform, as will very possibly be the case for large price cap carriers, such reductions should be considered in those companies' net change in intercarrier compensation revenues to be recovered from other sources. These cost reductions, plus increases in price cap carriers' SLCs to the existing caps, will offset a significant portion of their intercarrier compensation losses.

The Commission also questions whether it is "realistic to institute a regulated SLC for years to come, when market conditions may not allow carriers to charge such a SLC."¹⁶⁷ The implementation of SLCs and rate-of-return regulation are inexorably linked; thus, SLCs cannot be eliminated. The Commission initially developed SLCs as a means of recovering a portion of each ILEC's non-traffic-sensitive loop costs directly from customers. More recently the caps were raised to permit additional recovery.¹⁶⁸ For

Comprehensive Telecom Solution ("FACTS") Plan, along with equalizing SLCs between price cap and rate-of-return carriers at the price cap carriers' weighted average in each state.

¹⁶⁶ See *FNPRM* at ¶ 100.

¹⁶⁷ See *FNPRM* at ¶ 101.

¹⁶⁸ See *In the Matter of Access Charge Reform*, CC Docket No. 96-262, *Price Cap Performance Review for Local Exchange Carriers*, CC Docket No. 94-1, *Low-Volume Long Distance Users*, CC Docket No. 99-249, and *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Sixth Report and Order in CC Docket No. 96-262 and 94-1, Report and Order in CC Docket Nos. 99-249, and Eleventh Report and Order in CC Docket No. 96-45, FCC 00-193 ("*CALLS Order*") (rel. May 31, 2000) at ¶ 77 and ¶ 79.

rate-of-return ILECs, SLCs are an integral part of the total regulated cost recovery and rate design, and cannot be simply set aside. If SLCs were to be eliminated for rate-of-return ILECs, it would create even more pressure on universal service mechanisms since these ILECs would require another means of cost recovery. If ILECs face substantial competitive pressure, ILECs have the option of foregoing billing of the SLC. This option should continue.

B. A Benchmark Will Help Achieve Comparable Rates and Limit Reliance on USF.

The plan-sponsoring groups comprising the Rural Alliance each proposed that both local service rates and SLC rates be made more uniform nationwide to achieve comparability.¹⁶⁹ Since there are vastly different local rates and SLC levels nationwide, both local rates and SLCs must be considered on a combined basis as a composite end-user benchmark. From the customer's perspective, the aggregate price inclusive of both SLCs and local rates that is most important.

The Commission specifically asks if it should adopt some benchmark for local retail rates within the State jurisdiction.¹⁷⁰ The Rural Alliance supports imputing a benchmark rate into any replacement funding resulting from intercarrier compensation reform. If a State has already rebalanced rates, and an ILEC's local rates are higher than the local rate component of the benchmark, the ILEC should be allowed to decrease rates to the benchmark level and draw replacement funds. If an ILEC, for competitive reasons

¹⁶⁹ See *In the Matter of Developing a Unified Intercarrier Compensation Regime*, CC Docket No. 01-92, Ex Parte Brief by the Expanded Portland Group: A comprehensive Plan for Intercarrier Compensation Reform, ("EPG Plan") (filed Nov. 2) at pp. 23-26. See also *ARIC Plan* at pp. 61-66.

¹⁷⁰ See *FNPRM* at ¶ 108.

or otherwise, decides to leave its basic rates below the benchmark level, the composite benchmark will be imputed in the calculation of a company's receipts under the revenue replacement mechanism. In this manner, comparability standards will be met nationwide and the ILEC's end-users will not be unjustly treated for a State commission having previously taken appropriate action.

The Rural Alliance further suggests that the local rate component of the benchmark be set at the RBOC average urban rate and the SLC component of the benchmark be set at the current SLC caps. Rather than manage the multitude of rate cases that would result from setting nationwide local rates, an administratively simple and consistent procedure should be adopted by all States to facilitate local rate changes. If a State commission refuses to allow an ILEC to raise local rates, the ILEC and its customers should not be unduly penalized.¹⁷¹

Use of such benchmarks will limit the demands for replacement funds required to offset intercarrier compensation reductions. Inclusion of a benchmark will also appropriately recognize the rate rebalancing (i.e., increased local rates and reduced intrastate access rates) that has already taken place in several States. To implement intercarrier reforms without addressing local rate rebalancing would unfairly disadvantage those States that have taken appropriate action and those States that are net payers into the USF. Imputation of benchmarks would give ILECs the flexibility to charge retail rates less than the benchmark to meet competition, while assuring that

¹⁷¹ States are encouraged to adopt the federal model and approach. If a State decreases intrastate access charges and or reciprocal compensation rates and does not allow a company to increase local rates to the appropriate local benchmark level, then the company should be allowed to add another Federal charge to the customer bill to make up the difference.

qualifying companies receive replacement revenues only after implementing retail rates comparable to other companies nationwide.

C. Rate Averaging and Rate Integration Requirements Are Not Being Met Today.

In the *FNPRM*, the Commission seeks comment on whether it needs to take additional steps to address section 254(g) requirements regarding rate averaging¹⁷² and rate integration¹⁷³ for nationwide IXC's.¹⁷⁴ The Commission observes that nationwide IXC's, such as AT&T, which offer long-distance services in both urban and rural areas must compete with more localized long-distance carriers, such as the RBOCs, that have no such requirement. The Commission also is concerned about the impact on price and choice for rural consumers.¹⁷⁵ While attention to issues concerning rural consumers is appreciated, the Commission's attention to rate averaging and rate integration at this juncture is unnecessary given the long-existing calling plan decisions of IXC's, and is largely irrelevant considering the pending acquisition of nationwide IXC's by RBOCs. In addition, with the unification of intercarrier compensation charges, any disparities in wholesale access rates will be significantly reduced.

1. *The Toll Rate Averaging Requirements in Federal Law Have Never Been Strictly Enforced.*

¹⁷² 47 C.F.R. § 64.1801; *See also In the Matter of Policy and Rules Concerning the Interstate, Interexchange Marketplace*, CC Docket 96-61, Report and Order, ("Geographic Rate Averaging Order") 11 FCC Rcd at 9568-69, ¶ 9, 9574, ¶ 20.

¹⁷³ 47 C.F.R. § 64.1801; *See also Geographic Rate Averaging Order* at ¶ 52.

¹⁷⁴ *See FNPRM* at ¶ 86.

¹⁷⁵ *Ibid.*

The plain meaning of section 254(g) of the Act is clear and unambiguous that IXC's should engage in retail rate averaging to ensure rate comparability:

[t]he rates charged by providers of interexchange telecommunications services to subscribers in rural and high cost areas shall be no higher than the rates charged by each such provider to its subscribers in urban areas.¹⁷⁶

The Commission is thus directed under section 254(g) to require geographic *retail* rate averaging. The section does not require geographic *wholesale* rate parity.

Despite the law, the requirements of section 254(g) have not been followed by IXC's. A recent analysis of IXC calling plan availability shows that many beneficial calling plans are not being offered in rural, high-cost areas. Several billing agencies engaging in direct and third-party billing for AT&T shows that neither AT&T's Unlimited Plus Plan¹⁷⁷ nor its One Rate® 7¢ Plus Plan¹⁷⁸ is offered to RLEC customers as advertised. Instead, rural customers are offered the AT&T One Rate® Simple Plan.¹⁷⁹ Under this plan, rural customers pay 22¢ per minute more than their urban counterparts on the One Rate® 7¢ Plus Plan. For a customer who makes 500 minutes worth of interstate calls per month, the customer would spend just \$29.95 per month if the AT&T Unlimited Plus Plan were offered, but that same customer would spend \$145.00, or five times more, on the AT&T One Rate® Simple Plan. This example shows that rates are

¹⁷⁶ 47 U.S.C § 254(g).

¹⁷⁷ AT&T Unlimited Plus Plan offers unlimited long distance service 24 hours a day, seven days a week for a fee of \$29.95 per month.

¹⁷⁸ AT&T One Rate® 7¢ Plus Plan, which offers 7¢ per minute on all long distance calls 24 hours a day, seven days a week for a fee of \$3.95 per month.

¹⁷⁹ AT&T One Rate® Simple Plan offers the rate of 29¢ per minute for all domestic long distance for no monthly fee.

not currently uniform between urban and rural areas. Even so, the Commission has not taken action.

Under the requirements of section 254(g), the nationwide IXC's are required to average retail rates regardless of any existing access charge disparity. That having been said, the unification of wholesale rate levels on a company-by-company basis will greatly mitigate the existing wholesale rate disparity. As intercarrier compensation reform narrows the gap between various LEC's access rates, costs for nationwide IXC's will become more uniform and compliance with section 254(g) will become easier.

2. *Intercarrier Compensation Rates Recover Interconnection-Related Traffic-Sensitive Costs.*

In a related matter, the Commission questions whether section 254 could be interpreted such that the high costs of local switching and transport could be recovered from universal service.¹⁸⁰ The statutory requirement of section 254 and the underlying public policy sustaining this section have not been altered by technological changes. When section 254 was enacted in 1996, Congress may not have anticipated the rapid pace of Internet growth or the network changes in response to technological evolution. Congress wisely chose to focus on the availability of *services to customers*, not on the technological network choices made by service providers. Congress was well aware that the higher costs of providing rural telecommunications service were related to the higher costs of providing a rural local switching and transport network. These cost differences were a result of the geographic and demographic characteristics of rural areas.

¹⁸⁰ See FNPRM at ¶ 86.

Long before section 254 was enacted, the Commission, together with State regulators, implemented a rational rate design for cost recovery in a manner promoting universal service in rural areas. The regulators recognized that costs were incurred to provision a total network as opposed to isolated costs for local service, intrastate toll service and interstate toll service. As both the Commission and the State regulators understood, the joint and common costs necessary to operate a network are neither categorized as interstate nor intrastate until the application of the jurisdictional allocation process prescribed in the Commission's Part 36 Rules, as adopted pursuant to Federal-State Joint Board consideration.

Despite advances in technology, the costs of building and maintaining rural networks have not disappeared. Some network usage, previously related to services provided by IXC's, is migrating to services provided by other carriers — namely wireless and VoIP providers. Nonetheless, these other carriers still require the use of the RLECs' networks to originate and terminate traffic as well as transport such traffic.¹⁸¹ The evolution in technology used by interconnecting carriers should not, as a matter of policy and law, result in inordinate increases in rural subscribers' rates.

If the costs associated with rural network interconnection should no longer be borne through traffic-sensitive rates, these associated costs cannot be recovered solely through increased charges to rural end users. Such a result would contradict the comparability requirement in section 254. The Rural Alliance respectfully submits that the objective of this proceeding should be to redefine how rural network costs are

¹⁸¹ Such traffic could take the form of either wireless calls or any IP application.

recovered through a rational balance of USF and interconnection charges from those who benefit by utilizing the network.

D. Stricter ETC Designations Will Be Critical to Limit Unnecessary Universal Service Fund Growth.

The Commission also asks for guidance on the competitive neutrality of any new universal service mechanism with respect to eligible telecommunications carriers (“ETCs”) and competitive eligible telecommunications carriers (“CETCs”).¹⁸² The Rural Alliance supports stricter enforcement for ETC designations as a means of enforcing competitive neutrality and limiting inappropriate USF growth. A recently issued study on the Federal USF system reports that CETCs continue to be approved at a rapid pace, with no evidence that these ETCs advance the goal of universal service.¹⁸³ At current growth rates, the study warns that CETC support could ultimately exceed \$2 billion annually. The Commission has recently announced minimum permissive guidelines for State commissions to utilize in their consideration of CETC designation requests.¹⁸⁴ The Rural Alliance urges States to carefully consider these guidelines in reviewing CETC applications, and to apply these guidelines to the review of existing CETCs to ensure that they are fulfilling universal service obligations including Carrier of Last Resort responsibilities.

E. The Rural Alliance Examines the Efficacy of the Major Plans.

¹⁸² See *FNPRM* at ¶ 104.

¹⁸³ “*Universal Service: Rural Infrastructure at Risk*,” McLean & Brown (rel. March 2005) p. 4.

¹⁸⁴ See, generally, *In the Matter of Federal-State Joint Board on Universal Service*, CC Docket No. 96-45 Report and Order, FCC 05-719 (“*ETC Order*”) (rel. Mar. 17, 2005).

1. *The ICF Plan Will Result in Rural End User Rates that Are Not Comparable with Urban Rates.*

The ICF plan to increase SLC caps up to \$10 per line per month¹⁸⁵ will result in rural end-user rates that are not comparable with urban rates. In doing so, the ICF plan violates both the NARUC principle of preventing rate shock and ensuring the continuity of current penetration rates,¹⁸⁶ as well as the NARUC principle requiring comparable rural and urban rates.¹⁸⁷ Price cap carriers often charges SLCs well below the current SLC caps, especially for multi-line business lines, while rate-of-return LECs almost always charge SLCs at the cap.¹⁸⁸ Furthermore, if SLC caps were increased, most RLECs will be forced to raise SLCs to the new cap, while price cap carriers likely will not need to raise SLCs to the new cap. The exacerbation of the SLC differential will serve to increase the gap between urban and rural end-user rates.

In addition to the increased SLC caps, the ICF plan's proposal to geographically de-average SLCs will also contribute to disparate treatment between rural and urban consumers. The ICF plan contains almost no restrictions on how SLCs can be charged in the different zones. The plan states that "[t]here is no formula for the determination of SLC rates by zone. The ILEC may establish any set of zone rates that meets the revenue

¹⁸⁵ The CRTC's SLC cap increases to \$9.50, with an optional increase to \$10.

¹⁸⁶ See *NARUC Principles* VII. A.: "The transition to a new intercarrier compensation system should ensure continuity of existing services and prevent significant rate shock to end-users. Penetration rates for basic service should not be jeopardized."

¹⁸⁷ See *NARUC Principles* VII. C.: "Rural customers should continue to have rates comparable to those paid by urban customers. End-user basic local exchange rates should not be increased above just, reasonable, and affordable levels."

¹⁸⁸ See *ARIC Plan* at Appendix A for data. Only 5% of price cap companies charge SLCs at the multi-line business cap, while 94% of the National Exchange Carrier Association ("NECA") members charge the SLCs at the multi-line business cap. Calculations were performed by dividing the number of multi-line

limit, the per-line cap and increase limits....”¹⁸⁹ To meet competitive pressures in urban areas, price cap carriers will be motivated to charge rural customers the maximum SLC level, while urban customers will see only minimal SLC increases. The ICF plan’s deaveraging provisions will increase the rate disparity between rural and urban consumers, and would be a clear violation of section 254(b)(3) of the Act.¹⁹⁰

2. *The ICF Plan Will Put Unwarranted Pressure on the USF Funds.*

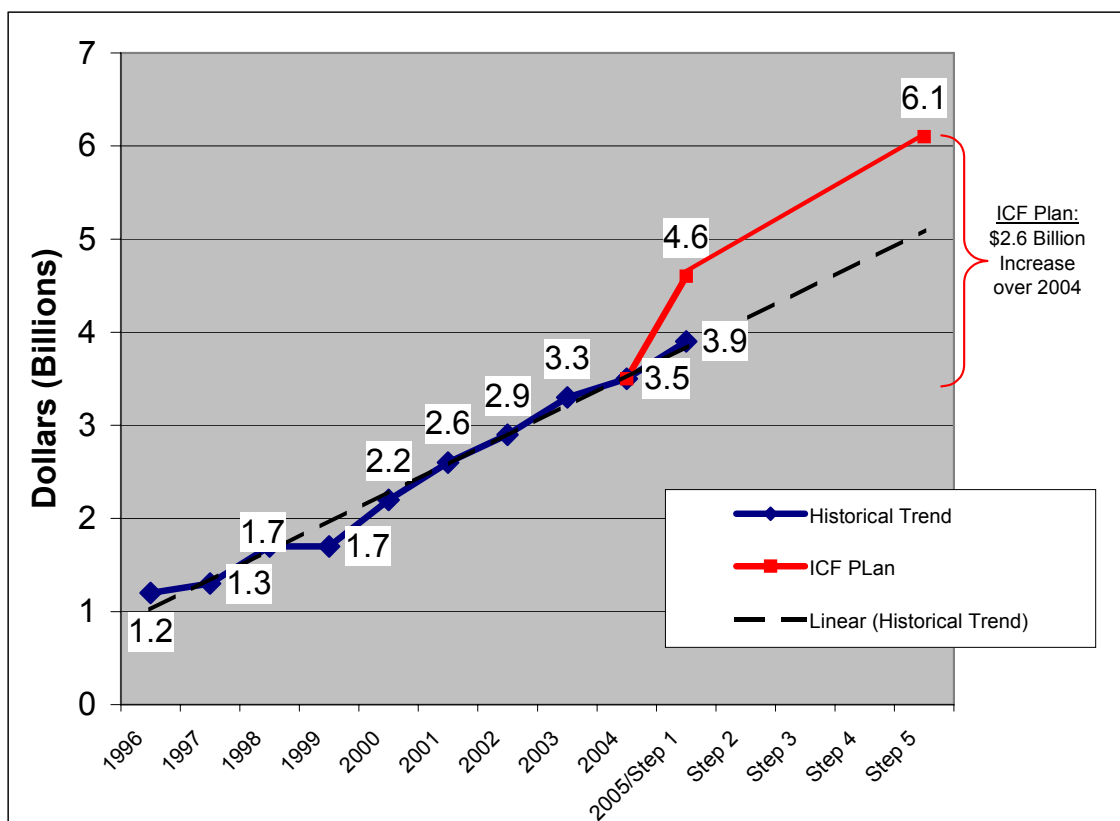
A report from the Progress & Freedom Foundation report indicates the high-cost fund is growing at a rate of about \$313 million annually, resulting in an estimated \$3.5 billion of high-cost funding in 2004.¹⁹¹ The ICF claims that implementation of its plan would add another \$2.6 billion annually to the USF at the start of step 5; thus, increasing the USF growth rate significantly, as shown in Figure 2 below. Because the ICF plan’s transitory uniform termination charge is to be cut in half in Step 6 and eliminated in Step 7, continued growth in high-cost funding requirements can reasonably be expected in the years following Step 5.

business lines charged at the SLC cap by the total number of price cap business lines to determine the percentage of price cap lines charged at the cap.

¹⁸⁹ See *ICF Plan* at p. 66.

¹⁹⁰ 47 U.S.C. § 254(b)(3).

¹⁹¹ Report available at: <http://www.pff.org/issues-pubs/books/050118usfreport.pdf>. See Report, pp. 16, 107. The Progress & Freedom Foundation, according to its website, is a nonprofit “market-oriented think tank that studies the digital revolution and its implications for public policy.” The Foundation states it is an “effective voice for market-oriented policy” supporting positions such as deregulation of communications markets including broadband, protecting “rich digital content” and explaining the need for lower taxes on telecommunications markets. Its supporters include BellSouth, Cellular Telecommunications & Internet Association, Comcast Corporation, Level 3 Communications, MCI, Nextel Communications, Qwest Communications, SBC Communications, United States Telecom Association and Verizon Communications.



Source for Historical Trend: Progress in Freedom Report at p. 16.

Source for ICF Plan: ICF ex parte December 6, 2004.¹⁹²

Figure 2. High-Cost Support Payments (1996-2005) and ICF Plan Estimates

The ICF Plan requires more USF than other plans identified in this Notice because more revenue is being displaced by the reduction of intercarrier compensation rates to zero. The enormous burden that the ICF’s bill-and-keep regime would place on the high-cost program would risk growing the fund to potentially unsustainable levels and would violate NARUC’s principle to minimize the impact on universal service support.¹⁹³

¹⁹² Support increases in Steps 1 and 5 are added to the estimated 2004 high-cost support level shown on the Historical Trend line.

¹⁹³ See *NARUC Principles* VII. D.: “Any intercarrier compensation plan should be designed to minimize the cost impact on both federal and State universal service support programs.”

3. *Some ILECs Will Likely Have a Net Windfall if the ICF USF Plan Is Implemented.*

The ICF plan proposes that revenue losses from access services and interconnection transport be recovered from end users and, if necessary, from additional universal service support. For CTRCs, the plan also proposes that net revenue losses from reciprocal compensation and interILEC settlements be recovered in this manner.¹⁹⁴ For CTRCs it is reasonable to receive replacement revenue for reciprocal compensation decreases, as these companies are likely to be net recipients of reciprocal compensation under today's arrangements. On the other hand, price cap ILECs are likely net reciprocal compensation payers as these ILECs often serve urban areas and frequently interconnect with Competitive Local Exchange Carriers ("CLECs") handling ISP-bound traffic. The rate reductions under the ICF plan will represent substantial cost savings to these companies, in the form of reduced intercarrier compensation payments. Meanwhile, for RBOCs that provide intraLATA toll service and pay access charges to other ILECs, the ICF plan does not account for savings due to the elimination of access expense. For situations where such RBOCs are not subject to imputation provisions or competitive pressures, retail toll rates may not track with access reductions, thus resulting in yet another windfall.

In determining the revenue an ILEC may recover from replacement sources, the ICF plan fails to account for an ILEC's access and reciprocal compensation expense reductions. Some large ILECs will likely benefit from substantial expense reductions due to intercarrier compensation payment decreases, yet would be able to recoup all

¹⁹⁴ See *ICF Plan* at p. 48.

reductions in their current revenues from either end users or USF. In failing to account for bill and keep's effects on an ILEC's expenses, the ICF plan would allow some ILECs to experience unjustified windfalls, resulting in unreasonable increases in end-user rates and/or USF.

4. *Western Wireless' High-Cost Support Levels Will Result in Insufficient Funding Levels.*

The widespread deployment of DSL technology by rural carriers has played an important role in breaching the so-called "digital divide." Even so, CMRS carriers are attempting to "turn back time" to when only voice service was available. Western Wireless, in its intercarrier compensation plan, proposes to reform universal service to base funding on least-cost technology:

Replace all existing USF mechanisms with a unified high-cost universal service mechanism that would be fully portable to all designated ETCs operating in a geographic area, and that would calculate support for all eligible carriers based on the forward-looking economic costs of providing the supported universal service in an area using the least-cost technology.¹⁹⁵

When CMRS carriers promote least-cost technology, they are advocating for funding of effectively a voice-only network. Support based on least-cost technology will likely be insufficient to provide comparable broadband access to advanced services.

Calculation of support based on "forward-looking economic costs" using "least-cost technology," as Western proposes, not only risks putting rural consumers back on the wrong side of the "digital divide," but also runs afoul of the Act. Section 254(b) of

¹⁹⁵ See *Western Wireless Plan* at p. 3.

the Act directs the Commission to base policies for the preservation and advancement of universal service on the following principles.¹⁹⁶

While broadband is not a supported service as defined in section 254(b), the Rural Alliance believes that support should be provided to carriers providing both the required supported services and access to advanced service. Indeed, the Commission stated, that the USF should create no barrier to the deployment of plant capable of providing access to advanced service.¹⁹⁷ As applications continue to migrate to an Internet Protocol (“IP”) network platform, a robust broadband network is essential. Any “least-cost technology” that cannot support access to advanced services, or that can only do so by degrading service to other customers,¹⁹⁸ should not become the basis for support calculations.

5. *The CBICC Proposal Disadvantages Rural Customers and Is Not Competitively Neutral.*

CBICC proposes that intercarrier compensation losses will be made up through a combination of universal service and increases in end-user charge supplements. The CBICC proposal places no limit on the increases in end user charges that an RLEC would impose to make up this revenue loss, stating, “[U]se of USF funds will last as long as necessary to phase-in a carrier’s end user charge supplement at no more than 50 cents per year.”¹⁹⁹ The CBICC proposal would pressure high-cost RLECs to increase local service

¹⁹⁶ 47 U.S.C. § 254(b)(3).

¹⁹⁷ See *In the Matter of Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Order and Order on Reconsideration, FCC 03-170 (rel. Jul. 14, 2003) at ¶ 13 (citations omitted).

¹⁹⁸ For example, in order to provide broadband services to their customers, CMRS carriers sometimes link several CMRS channels together, thereby degrading service to each customer.

¹⁹⁹ See *CBICC Plan* at p. 2.

rates to levels that violate the “reasonably comparable” provision of section 254(b)(3).²⁰⁰

Additionally, CBICC’s proposal to apply end user charge supplements “initially to business customers” is meant to place ILECs at a competitive disadvantage relative to CLECs that generally target business customers. Such a discriminatory provision is not competitively neutral and should be discarded.

²⁰⁰ See U.S.C. 254(b)(3).

IV. THE COMMISSION SHOULD CLARIFY THE APPLICATION OF ITS EXISTING INTERCONNECTION RULES TO COMPLY WITH EXISTING LAW.

The Commission is exploring whether to adopt new network interconnection rules. In this section, the Rural Alliance addresses the multitude of issues raised by the Commission in this regard. The Rural Alliance maintains that the Commission should not make wholesale changes to its existing rules, but rather should clarify those rules consistent with existing statute to avoid disruptions in the market.

A. Rules Should Accurately Reflect Cost-Causation Principles and the Act's Intent.

1. *Unfair Network Obligations that only Benefit Other Carriers Should Not Be Imposed on RLECs.*

The rules that establish the rights and responsibilities between and among carriers for network interconnection will remain a fundamental component of any intercarrier compensation framework. The Commission is properly concerned that provisions for monetary compensation between carriers, if not structured correctly, could result in the “ability to shift costs to competitors through intercarrier charges” which could distort “the competitive process.”²⁰¹ Network interconnection rules present exactly the same concerns if carriers are allowed to impose anti-competitive and unfair network burdens on network providers.

Without proper constraints, retail service providers will simply design their service offerings to force network providers to internally absorb the cost of providing network functions. The more network responsibility a service provider can push onto a

²⁰¹ See ICC NPRM at ¶ 16.

network provider, the more the service provider will be competitively advantaged to the detriment of the network provider. Some of the proposals currently before the Commission create particularly dangerous requirements that would unfairly and improperly burden RLECs by shifting network responsibilities through the application of network interconnection rules. Proposals that benefit service providers and harm network providers by imposing unfair network interconnection rules should be rejected for the reasons set forth below.

2. *The Existing “Retail Service Provider Pays” Principle Should Continue to Apply.*

The current network interconnection rules are rooted in the principle that the retail service provider (“RSP”) benefits from the use of the network and thus is responsible for compensating network providers for such use. The Rural Alliance refers to this concept as “Retail Service Provider Pays.” Of course, an RSP’s customers also benefit and are therefore willing to pay the RSP for such retail service.²⁰² For the most part, existing network interconnection rules reflect the appropriate wholesale-retail relationships as well as the need to compensate the underlying network owners when an RSP utilizes those networks for a business purpose.²⁰³

²⁰² The discussion in the *FNPRM* at ¶ 17 suggests that the existing intercarrier plan is based on a “calling-party-network-pays” approach, but that description is not correct. For IXC calls, the party that provides the initial network to the calling party (*i.e.*, the LEC providing the originating access) does not pay, and has never paid, as the label would incorrectly suggest. It is the IXC as the retail service provider that pays, not the calling party’s network provider. CMRS providers have twisted the “calling-party-network-pays” concept in state commission interconnection proceedings to suggest absurdly that LECs should pay terminating local carriers for IXC retail services. Again, IXCs are the retail service providers and should pay.

²⁰³ This approach would also make sense if applied to Internet Service Providers (“ISPs”) and dial-up ISP calls. The ISP is the retail service provider; it is the service provider causing costs to be incurred in support of its ISP service, and it should have a responsibility to compensate LECs for the network facilities that LECs must provision to deliver ISP traffic to the ISP. If the retail service provider/cost causation approach were applied to ISPs, there would be no problem with the current rules with respect to imbalances in traffic

Unfortunately, some parties have either forgotten or refuse to recognize the “Retail Service Provider Pays” foundation for the existing rules and have attempted to distort the meaning of these rules. These parties assert that this fundamental, common sense principle is broken and must be abandoned. A departure from this fundamental principle would be a mistake and would lead to a new set of “loopholes” and uneconomic incentives. If the correct application of the existing rules were confirmed, as described herein, these rules would continue to provide a reasonable, competitively fair basis to properly reflect the rights and responsibilities of network carriers.

3. *Rules Must Continue to Recognize Differences between Access and Reciprocal Compensation.*

Since IXC's without direct physical connectivity to their retail customers continue to exist, the current compensation framework, with separate and distinct structures for local interconnection and exchange access, must continue to exist to reflect the fundamental and inescapable difference between local interconnection and exchange access service.²⁰⁴ As long as this distinction exists, all rules, including network interconnection rules, must recognize this profound difference in interconnection scenarios. Any attempt to impose the same intercarrier framework on both IXC calls and local exchange carrier calls would result in an incongruous and logically flawed plan.²⁰⁵

for terminating networks that attempt to avoid transport and termination costs of ISP-bound traffic. *See ICC NPRM* at ¶ 90.

²⁰⁴ Under historical and existing industry structure and definitions, “toll” calls are interexchange service calls.

²⁰⁵ A single approach may make sense only if the distinction between IXC's and LEC's were somehow completely removed and the equal access requirement eliminated, in which case there would be only “carriers.” There does not appear to be any proposal to do away with IXC's at this time. Such a change would be a dramatic departure from current industry structure and would presumably impose new and

Interexchange (toll) calls are subject to the exchange access framework. An IXC is the RSP of long distance service to the end user customer. Since the IXC does not have a physical connection to its end user customers, it must purchase originating and terminating access services from one or more LECs while using its own network in the middle. An IXC's relationship with a LEC is not reciprocal. LECs provide origination and termination for IXCs' customers, but IXCs provide no reciprocal function for the LECs' customers. The IXC is the entity that sets the retail terms and conditions of service, offers and provides the service to the end user, bills the end user for the long distance service (or has another entity bill on behalf of the IXC), and keeps the service revenue. The IXC and its end user customer are the beneficiaries of the call; the end user pays the IXC; and the IXC pays the LEC(s) for the origination and termination functions provided. The IXC could not provide its end-to-end service without using the LECs' facilities. Under any rational system, the IXC must compensate the LECs for the use and the operational integrity of their networks.

In contrast, local exchange service exists when a carrier uses its own network to originate the call and either another local carrier's network or its own network to terminate the call. Local exchange service calls do not involve an IXC or an IXC service offering. The local carrier, itself, is the RSP to the originating end user and thus must pay for termination functions provided by other LECs or CMRS providers. As the RSP, the local carrier decides under what conditions it will offer and provide this service. The local carrier bills the end user any applicable charges and keeps the revenues. Under the

extraordinary service obligations on LECs to begin to provide the services to their end users that IXCs currently provide.

Commission's construct of section 251(b)(5) of the Act, following a request for interconnection between competing carriers, such local exchange calls are subject to the Commission's Part 51, Subpart H "reciprocal compensation" rules.

These two different service and carrier relationships cannot be logically "harmonized" under a single network interconnection framework, even though the pricing may be unified.²⁰⁶ Access calls under section 251(g) of the Act are separate and distinct legally from reciprocal compensation calls under section 251(b)(5)²⁰⁷ as described in this section of these Comments. In addition, two different network interconnection scenarios apply to interexchange and local exchange service calls.

Any attempt to apply a reciprocal compensation framework to IXC calls would be nonsensical. Under such faulty logic, LECs would be responsible for the switching and transport of IXC retail service calls to a "point of presence" with the IXC, *free of charge to the IXC*. No business or public policy principle could justify why a LEC would, *free of charge*, incur costs to deliver traffic to IXCs. The IXC benefits by offering the service to the public; the IXC bills and collects charges from the end user; and the IXC receives the revenue generated from the call.

²⁰⁶ See *FNPRM* at ¶ 97.

²⁰⁷ *Id.* at ¶ 79. Some carriers in state commission interconnection proceedings have attempted (using a misapplied "calling-party-network-pays" concept) to suggest illogically that a single call can somehow be subject both to access under section 251(g) of the Act and reciprocal compensation under section 251(b)(5) of the Act. The Commission correctly observes in the *FNPRM* that calls subject to access, including intrastate access service calls, are "carved out" from the scope of section 251(b)(5) which includes traffic subject to the reciprocal compensation framework. *Id.* Accordingly, the scope of traffic subject to access charges is mutually exclusive from the scope of traffic subject to reciprocal compensation pursuant to the Act and the Commission's rules. Moreover, the Commission has clarified, in response to requests by wireless carriers, that IXC service calls terminated to wireless carriers are within the framework of the access, not the reciprocal compensation framework of section 251(b)(5). See *In the Matter of Petitions of Sprint PCS and AT&T Corp. for Declaratory Ruling Regarding CMRS Access Charges*, WT Docket No. 01-316, Declaratory Ruling, FCC 02-203 (rel. Jul. 03, 2002).

Only if the Commission eliminated distinctions between local exchange and interexchange services, eliminated equal access, and eliminated IXCs would a harmonized approach for access and reciprocal compensation make sense. Since such dramatic changes do not appear to be under consideration, local interconnection and interexchange service calls must be treated differently. Different treatment arises because of differences in interconnection scenarios, not because one carrier is discriminated against relative to another, as the ICF claims.²⁰⁸

4. *An ILEC Has No Interoffice Transport Obligation Outside of Its Network.*

Apart from a proper compensation framework for IXCs' use of local networks as discussed above, the current network interconnection rules also address a LEC's obligations for transporting and delivering local exchange service calls to another carrier's Point of Interconnection ("POI"). The discussion in the *FNPRM* regarding POIs and various requirements that may, or may not, apply to the establishment of POIs between local competitors also bears directly on these obligations.²⁰⁹

Some carriers have distorted the meaning and application of the current rules to propose the imposition of unwarranted service and network burdens and provisioning responsibilities on RLECs well beyond those actually required by law, by current rules, or under any prudent public policy. These participants are attempting to reflect these same distortions in new rules.²¹⁰

²⁰⁸ See *ICF Brief* at p. 9.

²⁰⁹ See *FNPRM* at ¶¶ 87-97.

²¹⁰ The RBOCs have, over the last several years, entered into bilateral interconnection agreements and arrangements with other carriers and have attempted to exploit their legacy access arrangements with RLECs and their central "transit" carrier roles. Of course, the RBOCs have no right to negotiate

The objectionable aspects of these proposals would, if adopted, impose other carriers' arbitrary interconnection choices on RLECs; thus, discriminating in favor of the requesting carrier to the detriment of the RLEC. Under such unfair proposals, RLECs would incur extraordinary costs to transport local exchange calls to distant points — beyond the point that any other local exchange call would be transported and delivered. Frequently, the interconnection points are beyond the geographic area in which local exchange service calls are both originated and terminated, and beyond a point within the ILEC's network.

a. RBOC Interconnection Requirements Should Not Be Imposed on RLECs.

RBOC service offerings and network arrangements cannot be extended to RLECs, because an RBOC's network arrangements and service offerings do not translate logically into the operations of the typical RLEC. RLECs typically define the scope of their local exchange service offerings in terms of limited geographical exchange areas. As such, the end users physically residing in and obtaining local exchange service in one exchange area are provided local calling to all other users in that exchange area. Additionally, the networks of RLECs are many times smaller than RBOC networks and do not overlap geographically with those of the RBOCs.

One such attempt to extrapolate RBOC network responsibilities to RLECs is the inappropriate application of the single POI rules to RLECs. Under a single POI concept, RLECs would be forced to transport non-local calls to other carriers' distant POIs,

interconnection on behalf of other ILECs, and the agreements that RBOCs have with other carriers cannot and do not bind ILECs. Nevertheless, the RBOCs' interconnecting partners have attempted to impose their bilaterally designed arrangements unlawfully on the RLECs. As discussed later in these comments, the terms and conditions of multi-party arrangements requires additional and special attention to guard against

usually located on the RBOC's tandem. The effect would be that non-local calls would be included in an RLEC's local service offerings.²¹¹ Under these proposals, the RLEC would be responsible for transport beyond where the RLEC currently has any local call responsibility.

End users may also be provided with a local calling service to a limited number of immediately neighboring exchanges, which are usually selected based on a demonstrated community of interest. To provision the local calling service to the neighboring exchange, the LEC must deploy trunks between the original exchange area and the exchange area with extended calling. In circumstances involving local calling among multiple exchanges, there may be trunking through a locally operated tandem to connect the exchanges. Typically, the geographic scope of local calling extends a distance between 25 and 50 miles.

b. Illogical Transport Obligations Result When RBOC Rules Are Applied to RLECs.

To demonstrate the infeasibility of applying RBOC rules to RLECs, consider an example where an RLEC operates an exchange neighboring an RBOC exchange between

RBOCs and other large carriers using their size and already established arrangements to impose anti-competitive conditions on RLECs.

²¹¹ The end users are able to complete calls transported to distant locations by subscribing to IXC services, not LEC services. An RLEC's involvement in the provision of interexchange services is limited solely to the provision of originating access services to the actual IXC service provider. While some RLECs may have long distance affiliates that provide IXC services through contracts with an underlying facilities-based IXC, they do so through separate IXC affiliates. Not all RLECs offer IXC services, and there is no requirement for any LEC to provide such IXC service to their end users. In any event, IXC service is fundamentally different in many critical ways from local exchange carrier services. As discussed more in the text above, the *FNPRM* does not fully recognize this continuing, fundamental difference. Any approach that would attempt to impose a single framework to both local exchange calls and IXC calls would be logically flawed.

which the two incumbents have decided to provide local calling.²¹² While there are several options available to the provisioning incumbents, the most widely used methods involve each ILEC provisioning trunking facilities to the border point between the two exchanges for the exchange of local traffic. As such, the transport is shared roughly on an equal basis, and the RLEC's responsibility extends no further than the border between the two exchange areas. The RBOC may, according to its own internal network design, route trunks to its own local tandem or may route trunks directly to the end office included in the local calling between the two ILECs. Regardless, the RLEC does not incur greater or lesser costs depending on the RBOC's network design choices.

Now, assume a CLEC competes with the RBOC for local service in an exchange area, but does not deploy network facilities or services in that local exchange area.²¹³ The CLEC desires only to interconnect at an RBOC tandem office, which is typically located some distance away from the exchange areas where the local calling takes place.²¹⁴ Because the CLEC has opted not to deploy local facilities, the possibility exists that an RBOC end user's call to a CLEC end user must be transported to the distant tandem and then back, even though the two end users are physically located across the street from each other.

A misplaced application of rules has resulted in the RBOC being responsible for hauling this traffic back and forth. Under this approach, the remaining RBOC customers are shouldering the transport costs to the benefit of the CLEC's customers — a

²¹² There are obviously other arrangements and examples, but for the purpose of demonstrating the flaws in the proposals, a simple example is both relevant and widely prevalent.

²¹³ For the example that follows, the discussion and issues could equally apply to CMRS providers.

fundamentally unfair result. The costs should be borne by the carrier, in this case the CLEC, which caused these transport costs. Nevertheless, the RBOC and its customers should not be solely responsible.

The network interconnection “rules” proposed by some would apply these unfair requirements for transport within an RBOC network to RLECs. Under such proposals, when an RLEC’s customer calls a CLEC’s customer in the neighboring exchange, the RLEC could be responsible for transporting local calls all the way to the RBOC tandem where the CLEC has chosen to interconnect. In contrast, when the RBOC, rather than the CLEC, serves the end user in the neighboring RBOC exchange, the RLEC’s transport obligation for local calls is to deliver traffic to the RBOC at their mutual border. In addition to requiring RLECs to transport calls to a distant location at extraordinary cost, this interconnection rule would also force RLECs to purchase “transit” service from the RBOC.²¹⁵

There are two separate, but related, issues associated with the allocation of responsibilities where the competitive carrier does not establish its own network or utilize network services in the local calling area where calls are actually originated and terminated: (1) whether an individual ILEC should be required, at its own cost, to transport competitive carrier traffic to a distant location POI within its own network but beyond the local calling area; and (2) whether an RLEC should be required, at its own

²¹⁴ The RBOC tandem office may be located hundreds of miles away from the local calling area.

²¹⁵ Transit Service is a curious aspect of the ICF proposal. Under the plan, intermediary LECs such as RBOCs (the same carriers that want to do away with intercarrier compensation) may remain as the only carriers that continue to receive intercarrier compensation. The possibility exists that the bilateral actions of CLECs and CMRS providers with Bell companies could be imposed in a manner to force RLECs to obtain services involuntarily from RBOCs. In a competitive world, two carriers cannot bilaterally force a third carrier to obtain transit service from a RBOC.

cost, to transport competitive carrier traffic to a distant location POI established within some other ILEC's network at a point not only beyond the local calling area but beyond the network of the RLEC. The answer to both questions is "no." If a carrier designs its service offerings and network so that a local call between neighboring local exchanges must be transported to and from the actual local calling area, then the carrier that designed this service must be responsible for the extraordinary costs. Proposals that impose unwarranted and disproportionate transport obligations on RLECs, well beyond those required by any standard of fairness or public policy, must be rejected.

c. The Application of the Single POI Concept to Rural Local Exchange Carriers Is Illegal.

In response to the *ICC NPRM*, CLECs and CMRS providers argued that they should be allowed to establish a single POI per LATA, but they omit facts relevant to a complete analysis.²¹⁶ First, the concept was developed for application only to RBOC territories.²¹⁷ The Commission cites the section 271 proceeding with SBC as an example of the genesis of the single POI per LATA standard.²¹⁸ Second, the Act and Commission rules only require that an ILEC establish an interconnection point with a requesting

²¹⁶ *Id.* at ¶ 89. LATAs were established as a basis for the former RBOCs and AT&T to divide their assets at divestiture. Many, but not all, non-Bell company LECs were simply associated with LATAs for this purpose. Some non-Bell company LECs are not associated with any LATA, and there is no requirement that the Rural Alliance is aware of that requires any RLEC to continue to be associated with a LATA. The perpetuation of LATAs serves the competitive interest and advantage of RBOCs in a competitive world because they designed these areas based on their specific network design and thereby accommodated their specific operations.

²¹⁷ The underlying cases that have led to the notion of a single POI were all RBOC proceedings. The requirements were meant to apply to the single RBOC under review. Examples of such review include a section 271 proceeding involving the imposition of conditions that are the result of the continuing resolution of an anti-trust case against that RBOC or an arbitration proceeding between an RBOC and a requesting carrier. Proceedings conducted against an RBOC (interconnection arbitrations and 271 proceedings) do not establish interconnection requirement for other carriers. These proceedings simply established where the POI should be for that specific RBOC.

²¹⁸ *See FNPRM.* at ¶ 87 and note 276.

carrier “at any technically feasible point *within the carrier’s network*.”²¹⁹ The CLECs and CMRS providers often omit the last phrase, “*within the carrier’s network*,” thereby suggesting incorrectly that any “technically feasible point” means on *any* carrier’s network.

Under the Act, no ILEC is required to establish a POI at a point *not* within that ILEC’s network. The proceedings cited as the genesis of the so-called single POI requirement *did not conclude* that an RBOC is required to establish a POI with a requesting carrier at a point outside that RBOC’s network.²²⁰ Yet, that is exactly what would be required of RLECs. A POI outside the RLEC’s network is not “a technically feasible point *within the carrier’s network*.”²²¹

The courts have confirmed that interconnection obligations are confined to the ILEC’s existing network and existing service arrangements.²²² In applying the Act’s “technically feasible” POI requirements to RBOCs, the Commission has determined that the CLEC should be allowed to interconnect *with the RBOC* at a single point of interconnection per LATA *with respect to that RBOC*. In discussing the meaning of the

²¹⁹ 47 U.S.C. § 251(c)(2)(B). This same requirement is included in the Commission’s rules at 47 C.F.R. §§ 51.305(a) and (a)(2).

²²⁰ The Oregon Court’s decision, even as the suggested “rule” would apparently apply only to a single RBOC, nevertheless concluded that no such rigid requirement exists: “Technical feasibility answers the question of whether a CLEC may interconnect at a given point, but it does not answer the question of how many points of interconnection a CLEC must have.” *U.S. West Oregon Decision* at p. 852.

²²¹ While there may be options for carriers to utilize the network of third parties as the means to design some form of “indirect” interconnection, it does not change the definition of POI or the requirement that indirect facilities be used to establish a proper POI. This subject is also discussed under the section addressing so-called “transit” providers.

²²² 47 U.S.C. § 251(h), emphasis added. Interconnection requirements for an incumbent LEC, under the most onerous application, only apply to the area in which it has an incumbent network. “For purposes of this section [251 of the Act], the term “incumbent local exchange carrier” means, *with respect to an area*,

RBOC decisions, CLECs and CMRS providers often ignore the *italicized* aspects of those decisions. The single POI “standard” applies solely with respect to the requesting carrier’s right to interconnect *with the specific RBOC to which the request is made*. RBOC interconnection at a single POI should not be misconstrued as the POI for other uninvolved parties such as RLECs.

The Act requires an ILEC to provide interconnection services and arrangements at least equal to those that the LEC provisions for itself, but does not require *superior* arrangements to be designed and provisioned at the request of a competitive carrier. The U.S. Supreme Court and the Eighth Circuit Court of Appeals have agreed.²²³ Yet, the proposals requiring an RLEC to provision extraordinary transport to distant locations for local calls would represent just such a superior arrangement.²²⁴ Forcing an RLEC to incur the costs to transport traffic to distant locations at the request of a competitive carrier is contrary to the law.

the local exchange carrier that (A) on the date of enactment of the Telecommunications Act of 1996, provided telephone exchange service *in such area*.”

²²³ See Iowa Utils. Bd. v. FCC, 120 F.3d 753 (8th Cir. 1997). This aspect of the *Iowa Utils. Bd.* decision was not modified by the Supreme Court in Verizon v. FCC, 122 S. Ct. 1753 (U.S. 2002) and remains valid law. On July 18, 2000, on remand from the United States Supreme Court, the United States Court of Appeals for the Eighth Circuit issued its opinion in Iowa Utilities Board v. FCC, 219 F.3d 744 (8th Cir. 2000) (“*IUB II*”). In this decision, the Eight Circuit Court of Appeals reaffirmed its earlier conclusion, not affected by the Supreme Court’s remand, that previous rules that would have required LECs to provision interconnection arrangements that are superior to those that the incumbent LEC provisions for itself are not required under the plain meaning of “at least equal in quality to that provided by the [incumbent] local exchange carrier to itself” 47 U.S.C. § 251(c)(2)(C). Even under its original rules that were subsequently overturned by the Courts, where the Commission had intended to require incumbents to provision superior arrangements, the Commission nevertheless made the requesting carrier responsible for providing compensation to the incumbent for the extraordinary costs. See *Local Competition Order* at ¶ 225.

²²⁴ In addition, the Ninth Circuit Court of Appeals, in the context of a request for interconnection from a CMRS provider, also confirmed that the interconnection obligations are established with respect to the LEC’s existing network. U.S. West v. Wash. Utils. & Transp. Common, 255 F.3d 990 (9th Cir. 2001) (“Sections 251 and 252 of the Act require ILECs to allow CMRS providers to interconnect with their existing networks in return for fair compensation.”)

Neither the Act nor Commission rules require an ILEC to offer and provision some new form of local exchange service, including transport to distant locations, simply because a requesting competitive carrier has opted to interconnect with another LEC at a distant point. RLECs neither offer nor provide local exchange calling services involving transport to distant locations (e.g., to the RBOC tandem used in the example set forth above). Calls involving transport to distant locations, beyond the local calling area or beyond the network of the RLEC, are offered and provisioned by IXCs as interexchange service calls.

The statutes and rules cannot be distorted to suggest that a RLEC should be required to establish a POI with a requesting carrier at a point not within the RLEC's network. If such a requirement were to exist, it would impose a more onerous interconnection obligation on rural carriers than applies to RBOCs, and indeed would be a more onerous requirement than required under the most stringent sections of the Act.²²⁵ Any attempt to improperly extend the RBOC single POI per LATA to RLECs must be rejected.

5. *Rules that Reflect Fair, Rational Policy Can Be Applied to All LECs.*

²²⁵ Carriers compete for customers in the same area and therefore their networks overlap in those areas in which they compete. By way of example, a CMRS providers' service area and network may cover multiple states or even the entire nation. RLEC networks, on the other hand, may cover only a single community. When a CMRS provider seeks to interconnect with an RLEC, the CMRS network generally overlaps the entire RLEC network area, while the RLEC's network only overlaps a very small portion of the competing carrier's network and service area. Because it is only the areas that overlap where the carriers will be competing with each other, it follows that the interconnection point must be within the area common to both carriers' networks. If a POI is on the network of one carrier (perhaps at a RBOC tandem), but far from the area in which the two providers' competitive services and networks actually overlap, an unfair and undue burden is created for the carrier whose network does not exist at the distant location. The Act states that interconnection points must be within the network of the incumbent.

In its discussion of network interconnection issues and the potential responsibility of carriers to transport traffic to POIs, the Commission asks whether there should be different rules for RLECs.²²⁶ The ICF's inclusion of special CRTC provisions recognizes that its proposal would otherwise impose unreasonable and unlawful transport requirements on RLECs. There is no need to consider separate and disparate interconnection rules for RLECs if existing rules are clarified and applied in a fair and rational manner, the potential provisions requiring RLECs to incur new costs to transport calls to distant locations are removed, and the requirement to interconnect at a technically feasible point within the ILEC's network is applied properly.

6. *All Carriers Should Be Required to Correctly Identify Terminating Traffic for Billing Purposes.*

The Commission seeks comment on whether the current rules and industry standards create billing records sufficiently detailed to permit the originating and terminating carriers to determine the appropriate compensation due.²²⁷ Although missing billing data can be caused for several reasons, there is a growing trend for carriers to avoid terminating compensation by transmitting calls without sufficient billing information. Despite the telecommunications industry's long-standing rules regarding identification of calls, some carriers appear to be altering call details and sometimes omitting Carrier Identification Codes ("CIC") and Operating Company Numbers

²²⁶ See FNPRM at ¶ 94.

²²⁷ *Id.* at ¶ 133.

(“OCN”), leaving the terminating carrier without sufficient information to bill intercarrier charges to the originating carrier.²²⁸

Some telecommunications players apparently are building business cases based on avoiding compensation to connecting carriers. Many RLECs terminate indirectly routed CLEC traffic without compensation because the ILEC has not been contacted by the CLEC regarding local traffic compensation under section 251(b)(5). An even more egregious situation exists when a CLEC permits a VoIP provider’s interexchange traffic to terminate over local facilities. In addition, it is widely believed that some CMRS carriers do not always provide accurate jurisdictional billing information.²²⁹

When carriers alter billing information, such as calling party information, call tracing is impossible thus putting national security at stake.²³⁰ The Rural Alliance believes the practice of stripping or altering billing information is unlawful and can be prevented by the Commission ordering all carriers to adhere to existing network billing specifications established by industry billing forums. Furthermore, the Rural Alliance believes the Commission has the authority to assess penalties on those carriers engaging in such unlawful business practices.

For terminating traffic delivered by an IXC via Feature Group D (“FGD”) trunks to a LEC tandem, the Rural Alliance believes that current rules and industry standards, if followed and enforced by the Commission, are adequate to generate billing records with

²²⁸ Kevin Maney, Andrew Backover, and Elliot Blair Smith, “Straightening Out the Story on Telecom’s Routing Game,” USA Today 28 Aug. 2003.

²²⁹ Susana Schwartz, “Improving Interconnect Between Wireless and Wireline Carriers,” Billing World and OSS Today Feb. 2005.

²³⁰ “Carriers Cheating Other Carriers,” Billing World and OSS Today Aug. 2003.

sufficient detail to enable proper billing of IXC access charges. Under the current procedures, the tandem LEC creates industry standard Access Usage Records (“AURs”) and provides these records to the terminating LEC. The terminating LEC uses these AURs to bill access charges to the IXC based on the CIC in the billing record.

For traffic delivered to a terminating carrier via the Feature Group C intraLATA toll network, the Rural Alliance believes the current rules and industry standards are inadequate to generate sufficiently detailed billing records to identify the originating carrier and determine appropriate compensation due. Only the first tandem service provider can identify the originating responsible carrier based on the incoming trunk group. Frequently, this traffic enters the LEC network and passes through several tandems before the call is delivered to the terminating carrier, and CIC information is often not passed from one tandem provider to the next.²³¹ The Rural Alliance believes that the Commission should create rules requiring the first tandem provider in the call path to create billing records identifying the originating carrier and the nature of the traffic. Furthermore, the first tandem provider should be required to make that billing information available to all LECs in the call path, not just the terminating carrier. The first tandem provider must record transiting traffic in order to bill its own transit service charges to the originating carrier. Consequently, these records are already being created and used within the tandem provider’s own billing systems.

While unified compensation rates eliminate the need for factors to apportion traffic between jurisdictions, such as the Percent Interstate Usage factor, a unified rate

²³¹ The Rural Alliance uses the term “tandem provider” generically in this description. According to the ICF proposal, the existing tandem providers will be transit providers. In other words, the same network functionality occurs regardless of whether the traffic is local or toll.

does not eliminate the need for the carriers to populate the Jurisdiction Information Parameter (“JIP”) field in the SS7 signaling record. The Ordering and Billing Forum (“OBF”) committee of the Alliance for Telecommunications Industry Solutions (“ATIS”) ²³² has *recommended* that the JIP be included in the SS7 datagram but did not *require* inclusion of the JIP.²³³ The JIP field determines the originating switch; thus, the originating carrier’s OCN can be identified. The capability to identify the originating switch and carrier is extremely important for CMRS roamer traffic, because the calling party’s CMRS carrier and the CMRS carrier owning the originating switch may be different. In addition, the JIP may also be used to determine the originating carrier when an ISP terminates long-distance traffic to a LEC.

To ensure that the JIP is populated where the technical capability exists, the JIP should be a mandatory parameter for all local number portability (“LNP”) capable switches. The technical capability to provide the JIP is inherent in all LNP-capable switches. If the originating switch is not LNP capable, the carrier with the subsequent LNP-capable switch in the call path should be required to populate the JIP, in accordance with ATIS standards.

²³² Alliance for Telecommunications Industry Solutions (“ATIS”) is a technical planning and standards development organization that develops and promotes technical and operational standards for communications and information technologies industry. ATIS is comprised of 21 industry committees, including the Ordering and Billing Forum. www.atis.org

²³³ “Impact of Wireless Number Portability on Wireline Service Providers,” OBF Issues Number 2349, (Dec. 2004). This issue describes the importance of the JIP in determining the originating switch, thereby carrier, due to intermodal number portability and number pooling. The OBF adopts Seven Rules for Populating the JIP that are set forth in the NIIF Reference Document, Part III, Installation and Maintenance Responsibilities for SS7 Links and Trunks produced by the ATIS sponsored Network Interconnection Interoperability Forum (“NIIF”).

The Rural Alliance believes the Commission should implement rules requiring all carriers to abide by the ATIS billing guidelines.²³⁴ In addition, the Commission should establish a procedure whereby all ATIS network architecture guidelines are submitted to the Commission for approval prior to implementation, which would allow the Commission to solicit appropriate industry comments through standard notice procedures.

7. *The Rural Alliance Examines the Efficacy of the Major Plans.*

a. Under the ICF plan, RLECs Are Denied the Right to Design their Own Networks.

The ICF establishes a new set of carrier rights and responsibilities by creating arbitrary definitions,²³⁵ limits on network configurations and new carrier obligations. These new responsibilities can harm carriers in at least two ways. First, some carriers could unilaterally design their network configurations and then require other carriers to incur extraordinary and competitively unfair costs to provision services and networks to support that unilateral design. Second, some carriers, most notably RBOCs and the carriers that have interconnection agreements with RBOCs, may attempt to design a network plan that denies smaller carriers their competitive right to design their own network configuration and service offerings without interference.

b. The ICF Plan Obscures the Wholesale-Retail Relationships in the Long-Distance Market.

Since access charges were instituted in 1984, the long distance market has been characterized by two distinct segments: (1) end-to-end retail service provided by IXC's to

²³⁴ A carrier could request a waiver from certain rules that are not applicable to its particular operations.

²³⁵ Such definitions categorize carriers and network configurations.

end-user consumers; and (2) wholesale exchange access service provided by LECs to IXC's. For originating long distance, the originating customer pays the IXC; whereas for 800 long-distance service, the terminating customer is responsible for paying the IXC. Through these arrangements, end users have a single point of contact for their long distance calling needs.

By eliminating nearly all forms of intercarrier compensation, the ICF plan would radically alter the nature of the long-distance market. The elimination of originating and terminating access would dramatically reduce IXC's per-minute costs of providing long-distance service, yet LECs would still provide physical access to customers for IXC's service. Even though the LEC provides an input to the IXC's product, the LEC would not be paid. In no other industry would retailers (such as IXC's) be allowed to provide customers a product or service using raw materials of another company (such as LEC's) without compensation.

Under the ICF plan, end-to-end long-distance service would necessarily be bifurcated, with each carrier billing for its segment of the call. The LEC would be forced to recover its origination cost from the customer physically connected to the LEC's network. For 800 service, the originating LEC must recover its cost by billing the originating customer because the LEC has no relationship with the terminating customer — an illogical and illegal result. In addition, the benefits of a single point of contact for long distance needs would be eliminated. Customers would be forced to contact multiple carriers to resolve billing and operational issues. Without a single party responsible for end-to-end calls, carriers will attempt to blame other carriers for problems.

c. Section 251(b)(5) Should Not Be Applied to All Interconnection as the ICF Suggests.

The Rural Alliance believes that the ICF's reading of the language in sections 251(g) and 251(b)(5) is clouded by the ICF's goal to eliminate intercarrier compensation. The statutes clearly preserve the access charge regime, as explained in Section IV. An intercarrier compensation framework based solely on reciprocal compensation, such as that proposed by the ICF, cannot be applied to all interconnection situations. The reciprocal compensation framework was designed to handle the exchange of traffic between two *local* networks. Reciprocal compensation applies when one carrier owns facilities used to originate calls, but must rely on another carrier's facilities to terminate its customers' calls to the second carrier's customer. By contrast, exchange access applies when the RSPs have no facilities physically connected to end users; thus, section 251(b)(5) does not apply.

Maintaining the access market is particularly necessary in view of the pending SBC-AT&T and Verizon-MCI takeovers, which, if approved, would give these RBOC giants tens of millions of interexchange customers previously with AT&T and MCI. These mergers make it even more critical to continue allowing LECs to recover the costs caused by IXCs. If access were eliminated, these massive, vertically integrated companies would have free use of all local networks for their newly acquired IXC businesses. Of course, these companies also would continue to control the local and long distance markets in their own expansive service areas. Yet these companies' market power in the circuit-switched environment would pale in comparison to the daunting power they would ultimately possess in the IP world. Given that IXCs still utilize LEC facilities, along with the imminent acquisition of AT&T and MCI by what are already

some of the nation's largest telecommunications providers, elimination of access charges is irrational and illegal.²³⁶

d. The ICF Plan Does Not Adequately Compensate Rural LECs for Intracompany Transport.

The rates the ICF proposes for transport are solely based on minutes of use and cannot adequately reflect the cost of terminating transport, which is both a function of mileage and of traffic load. For CTRCs, transport costs represent a significant portion of total network costs. CTRCs in many instances have significant miles of transport behind the ICF-defined edge. This intracompany transport, which frequently represents many more miles than the distance from the meet point to the edge, is uncompensated under the ICF plan. The edge thus creates an arbitrary differentiation between compensated and uncompensated transport within the same network.

e. It Is Unclear Which Customers Can Be Accessed When Traffic Is Brought to the ICF's Edge.

The ICF plan states that “[a] carrier shall publish its list of Edges and associated routing information in a public manner, such as on a website.”²³⁷ While it appears that CTRCs and non-hierarchical carriers must make their entire networks available, hierarchical carriers can decide which NPA-NXXs can be terminated for free once traffic is brought to the edge. For example, is the RBOC only responsible for delivering traffic to specific NPA-NXXs, the entire LATA, or the nationwide service area of the RBOC? The plan leaves the decision up to the whim of the RBOC involved.

²³⁶ The Rural Alliance notes that any elimination of exchange access and the charges associated with that service would have to be coupled with elimination of equal access provisions in section 251(g). Since access would cease to exist, it follows that obligations to provide customers with equal access to IXCs would also be discontinued, since LECs would no longer provide access services.

The situation proposed by the ICF is inconsistent with peering arrangements whereby access is gained to the entire address space of a connecting carrier. For the edge concept to make any sense, a carrier must be able to access the entire address space (all telephone numbers) of the RBOC's region. Otherwise, RBOCs would be able to manipulate the interconnection environment by limiting the address space available to connecting carriers.

f. RBOC-IXC Mergers Present Significant Issues with Respect to the ICF Plan Implementation.

As part of ICF plan's default rules for intercarrier traffic exchange, the plan provides that "[e]ach carrier will establish an "Edge" or "Edges" at the point or points at which the carrier will receive traffic for routing within its network."²³⁸ After the merger of an RBOC and IXC, the definition of carrier and the definition of a "network" becomes unclear. Where is the edge after the merger of a hierarchical LEC and a nationwide IXC? Will the RBOC that acquired the nationwide IXC now have an edge in each LATA? Since a carrier must receive traffic for "routing within its network," shouldn't the merged RBOC be required to receive traffic nationwide and terminate such traffic to any of its customers within the RBOC's home region? The ICF plan makes no provision for merged IXC-RBOC edges despite there being two such mergers pending. When asked how the edge would apply to a merged environment, ICF representatives have no answers other than to say the pending mergers do not affect the edge rules. Such responses are not only inadequate, but dangerous.

²³⁷ See *ICF Plan* at p. 5.

²³⁸ *Id.* at p. 4.

The ICF plan's default rules, coupled with the market power wielded by an RBOC, will result in unfavorable treatment of small LECs and their customers. Although the ICF plan categorizes the rules as default, it is unrealistic to suggest that a CRTC in negotiation with a large RBOC will be in a position to negotiate more favorable terms than the default rules. Furthermore, RBOC market power will only increase as RBOCs acquire IXC's to create massive, nationwide, vertically-integrated companies. The adoption of a negotiation-based plan without protections in place to address market power is merely a ruse.

g. The ICF's Edge Proposal Is Too Complex To Be Interpreted in a Consistent Manner.

While the notion of bill and keep might appear to embody elegant simplicity, there is nothing simple about the ICF Plan itself. The plan is presented in 82 pages of mostly single-spaced text, which contain edge rules, transiting rules, traffic imbalance rules and a multi-step transition to plan implementation, as well as formulations of two new high-cost support mechanisms and a new USF contribution methodology. The plan is supplemented by network diagrams depicting 15 different interconnection scenarios, though the most common scenario for rural areas, end-to-end long distance service provided by an IXC, is conspicuously missing.²³⁹

The complexity of the ICF Plan is confusing at best, and would lead the Commission to adopt rules that cannot be operationalized. The interconnection methodology proposed by the ICF is so complex that few people even understand how it applies. The numerous carve-outs and exceptions, detailed in the ICF network diagrams,

²³⁹ See ICF Plan, Appendix D at pp. 1-15.

will make the writing of uniform, generalized rules virtually impossible. For example, the plan contains inconsistencies in both edge placement and certain compensation obligations.

If the ICF believes this proposal can be successfully implemented, it should submit a set of proposed rules. Such a rule set would necessarily be much more detailed than is usually included in Commission rules. Furthermore, any new rules should not be so vague as to require negotiations; yet this is what is being proposed by the ICF.²⁴⁰ Default rules, with an option to negotiate more favorable terms, disadvantages small entities attempting to negotiate with large entities possessing market power.

Presumably either State commissions or the Commission will assume the role of arbitrating disputes arising from rule interpretation. The many questions that currently exist regarding how the plan is applied attest to the lack of clarity, inconsistencies and gaps in the ICF rules. If State commissions arbitrate the ICF rules, the industry may be faced with 50 different interpretations. If, on the other hand, the Commission is to decide how to apply the rules nationwide, then the Commission will have an overwhelming task indeed.

To implement the ICF plan, billing systems also will need to be totally rewritten. Considering the low intercarrier rates in the proposal, the cost of major changes to billing systems is not worthwhile. For CTRCs, the plan requires tracking of calls by type of carrier. A CRTC must know the type of carrier (another CRTC, a hierarchical carrier or a non-hierarchical carrier) serving the customer who originated the call in order to properly

²⁴⁰ See *ICF Plan* at p.2

bill. Billing in an LNP environment will require the development and maintenance of a database associating every telephone number and the type of carrier currently holding the number. The creation of more complex billing systems is not a prudent use of resources, especially when the CTRCs have to make the most substantial changes.

h. Western Wireless's Proposal Attempts to Impose Illegal Transport Obligations on LECs.

Western suggests that the Commission "should reaffirm its interconnection rules governing the exchange of traffic with wireless carriers, and should clarify that [...] (2) wireless carriers are entitled to 'local' interconnection arrangements based on the rating points for their customers, regardless of how traffic is actually routed."²⁴¹ A LEC's section 251(b)(3) toll dialing parity obligation means that when a toll customer makes an originating toll call, the LEC must route the call to the IXC of the originating toll customer's choice on interexchange facilities. Such calls are subject to access charges. The Act does not authorize the Commission to make intercarrier compensation dependent on how the wireless carrier chooses to rate its customer's retail calls.

Western also attempts to impose illegal transport burdens on RLECs:

"[E]ach carrier bears financial responsibility for delivering its originating traffic to another carrier's "edge," in a LATA, or (at the option of the originating carrier) to a mutual meet-point at a hierarchical ILEC's access tandem in the LATA."²⁴²

The Rural Alliance objects to any proposal that burdens an RLEC with financial responsibility for transporting traffic beyond the boundaries of its network. Such a

²⁴¹ See *Western Wireless Plan* at p. 2.

²⁴² *Ibid.*

proposal conflicts with section 251(c)(2), which limits ILECs' interconnection duties to interconnection on the ILEC's network "at any technically feasible point *within the carrier's network*."²⁴³

- i. *CBICC's Position that CLECs May Designate a Single POI per LATA Is Contrary to Law.*

The Rural Alliance disagrees with CBICC's assertion that existing interconnection rules contain a provision allowing CLECs to designate a single POI per LATA.²⁴⁴ Nowhere has the idea of a single POI per LATA been codified in the Commission's rules, nor does the Act require an RLEC to establish a POI at a point outside the RLEC's network. The Act only requires RLECs to interconnect on the RLEC's network "at any technically feasible point *within the carrier's network*."²⁴⁵ CBICC appears to understand that the single POI per LATA concept only has been applied in RBOC situations because CBICC makes the statement that rural carriers should not bear transport obligations beyond their service boundaries. As discussed previously in these Comments, the application of the single POI per LATA cannot legally be extended to RLECs.

B. Both Access Services and Transiting Services Are Covered Under the Duty to Interconnect.

Another issue that has engendered attention is the provisioning of tandem-switched services by carriers – primarily RBOCs, but also other providers – that operate

²⁴³ 47 U.S.C. § 251(c)(2), emphasis added.

²⁴⁴ See *CBICC Plan* at p. 3.

²⁴⁵ 47 U.S.C. § 251(c)(2)(B), emphasis added.

tandem switches across the country. The manner in which tandem-switched services have been defined, offered and priced in the ICF plan is suspect and likely impermissible under common carriage requirements. Namely, the assurances in Section 201 that all carriers must interconnect on fair, reasonable and not unjustly discriminatory terms would be violated if the ICF proposal (which creates an anti-competitive haven for the largest providers of so-called “transiting services”) were to go forth without modification.

1. Regulation of Tandem Services Is Important Because There Is Often No Alternative Provider.

The Commission asks in the *FNPRM* whether there is a need for rules governing the terms and conditions of tandem transit service offerings.²⁴⁶ The Rural Alliance stresses that rules are not only necessary, but critical to the continuation of viable services in all sectors of the nation (particularly rural America) since there is often no alternate provider of tandem services. A discussion of necessary rules must first be accompanied by a clear and objective understanding of the services comprising transiting services today and in the future. Since the ICF improperly lumps all tandem-switched services into the vast expanse of “transiting,” the specific services themselves have been muddled. The plan sponsors attempted to distinguish transiting from other intercarrier services to secure special treatment. Clearly these “transiting” services are among those intercarrier services that exist today and will exist well into the future.

Transiting services, through use of tandem switching and tandem transport facilities, are a vital component of both intercarrier compensation regimes in which the industry operates — interexchange services and local interconnection services. The

²⁴⁶ See *FNPRM* at ¶¶ 129 and 131.

transiting services under both systems are methods of “indirect” connection as prescribed in section 251(a).²⁴⁷ For interexchange services, the IXC often connects indirectly with LECs, especially in rural areas. In this type of connection situation, the IXC delivers its traffic to the tandem switch of an intermediary carrier, which then transports the traffic to the terminating LEC. The intermediary and terminating LECs charge the IXC for the access services that the IXC utilizes to serve its customers. The intermediary (the ICF would call it the “transit” provider) charges for tandem switching and tandem transport, while the terminating LEC charges for local switching and usually local transport. These services and charges are maintained in the tariffed access charge rate structure.

For local interconnection, transiting services are utilized when two non-ILEC carriers exchange local (not interexchange) traffic by way of an intermediary tandem provider. The transiting services of the “carrier in the middle,” or intermediary carrier, are necessary to facilitate interconnection between the carriers on either end. The intermediary carrier, in many instances, can control all competitive access to the carriers that subtend it. This type of transiting service only applies when the exchange of local traffic between two non-ILEC carriers requires transiting from a third-party provider to complete calls.

In local interconnection situations involving an ILEC, CMRS carriers may use transiting service for the termination of traffic. Originating traffic destined for a POI outside of the ILEC’s local service area is routed to the originating end user’s presubscribed interexchange carrier (“PIC”) via exchange access facilities. Transiting

²⁴⁷ 47 U.S.C. §251(a)(1) states that each “telecommunications carrier has the duty to interconnect directly or indirectly with the facilities and equipment of other telecommunications carriers.”

may also be used for voluntary EAS arrangements entered into between an ILEC and another carrier. In this situation, tariffed transit service could be elected by mutual agreement instead of building a direct connection between the two carriers. No matter whether the RBOC tandem and transit functions are used for exchange access or interconnection, these services are critical to the provision of telecommunications services in rural areas, and in providing these vital services, tandem providers are in position to control access to all other carriers subtending the tandem.

Given this background, the Rural Alliance addresses the Commission's questions regarding the application of rules to transiting services.²⁴⁸ The Rural Alliance believes that transiting services should be subject to rules just as rules apply to all other intercarrier services necessary for carriers to fulfill their interconnection obligations. An additional rationale for establishing tandem service rules is that these services are often essential to the existence of *any* telecommunications service in areas of the nation where no tandem service alternatives exist. Without protections, many areas of the country risk having no tandem transit provider or, at a minimum, face a market where the tandem transit provider could extract monopoly rents for its services. The ICF plan proposes just such an untenable scenario, in which transiting rates are allowed, but ultimately unencumbered by rule while most other intercarrier service rates are moved to bill and keep. The Rural Alliance believes that the ICF's treatment of transiting services could result in unintended consequences comparable in magnitude to the financial burdens associated with ISP-bound traffic.

²⁴⁸ See *FNPRM* at ¶¶ 129-132.

The potential for tandem providers to leverage their market power looms particularly large given the market consolidations occurring between RBOCs and national IXC's. Without intervention, the market dominance wielded by these merged entities would leave other carriers with no alternative but to pay whatever transiting rates are offered or face isolation and ultimately extinction. Thus, tandem transit services must continue to be available by tariff for interexchange services and local interconnection. The rates for these services should be cost-based and comparable to the standard ultimately determined for all intercarrier compensation in this proceeding.

2. ***Transit Service Should Be Provided Under Reasonable Rates, Terms and Conditions.***

The Commission further asks if there should be requirements for the provision of transit service obligations, and if so, whether there is legal authority for imposing such requirements if transit service rules are adopted.²⁴⁹ The Rural Alliance believes that the Commission has broad authority under sections 201(a) and (b) to prescribe rates and terms for transit service.²⁵⁰ As observed above, transiting services enable the indirect connection between two carriers utilizing the facilities of a third provider, a right provided for in section 251(a). Thus, the application of Section 251(b)(5) to ultimately justify the transiting-service proposal contained in the ICF Plan is faulty. Section 251(b)(5) cannot apply to interexchange traffic since it is not relevant in that context. Although transiting services enable the exchange of local traffic under section 251(b)(5), transiting services inherently are not reciprocal. Therefore, section 251(b)(5) does not apply.

²⁴⁹ See FNPRM at ¶¶ 121 and 127.

²⁵⁰ Terms and conditions for tandem providers must include the provision of accurate billing information.

Sections 201(a) and (b) provide direction for proper enforcement of common carrier services such as tandem transiting. Section 201(a) states that “it shall be the duty of every common carrier engaging in interstate or foreign communication by wire or radio to furnish such communication service upon reasonable request ... to establish physical connections with other carriers....”²⁵¹ Section 201(b) further requires that the services be provided on a just and reasonable basis, and finds that any attempt to provide the services in a discriminatory manner be declared unlawful.²⁵² These unambiguous passages provide ample direction for tandem providers: Wherever a carrier has transiting facilities available to provide indirect connectivity, the carrier has a duty to provide them in a fair, just and non-discriminatory manner.

Concerning transiting services rates, section 201(a) is again conclusive because it envisions the Commission’s right to govern both the “division of such charges” for the physical connections and the routes carriers establishes with each other. Similarly, 201(b) also requires fair and just charges for these services, and deems unjust or unreasonable charges to be unlawful.²⁵³ Consistent with its recommendation for all intercarrier services, the Rural Alliance believes that transit service rates should be cost-based, similar to those rates currently applicable to tandem switching and tandem-switched transport, and set forth in tariffs. Cost-based transiting rates will satisfy the concerns raised by the Commission as to limitations that tandem switch providers claim

²⁵¹ 47 U.S.C. §201(a).

²⁵² 47 U.S.C. § 201(b).

²⁵³ 47 U.S.C. §§ 201(a) and (b).

are needed to prevent traffic congestion and tandem exhaust.²⁵⁴ As long as the rates set for tandem transiting services are cost-based, transit providers will recover their costs; thus, it will be feasible to add capacity should tandem switches approach exhaustion.

3. *The Rural Alliance Examines the Efficacy of the Major Plans.*

a. The ICF Disregards Tandem Switched Transport as a Component of Exchange Access.

The ICF plan fails to recognize that tandem switched transport is a component of the exchange access service offered by LECs to IXC. Tandem switched transport enables an IXC to provide its end-to-end retail long distance service. For the exchange access interconnection scenario, tandem providers are paid access charges to provide this service.

b. The ICF's Tandem Transit Proposal Is Temporary and Inadequate.

The ICF plan attempts to create a misleading sense of stability by proposing to maintain regulation of transit service for a limited time period. This stability is short lived because the ICF then proceeds to eliminate the rate cap “[e]ffective July 1, 2013 (8 years from implementation as written).”²⁵⁵ The proposed removal of rate protections will leave smaller companies at the mercy of the transit provider, which would be free to charge whatever rate it wishes. In reality, small carriers may be unable to obtain transit service at any price upon expiration of the plan. The ICF reserves the right to argue that the Act does not compel the offering of tandem transit service.²⁵⁶ Thus, the requirement to provide transit service and the regulation thereof may not remain in effect. The ICF

²⁵⁴ See FNPRM at ¶127.

²⁵⁵ *Ibid.*

²⁵⁶ *Id.* at footnote 29 p. 25.

plan's transiting conditions create a false sense of protection to lull regulators into acquiescence, while providing no real protection going forward.

C. CMRS and LEC Interconnection Rules Should Reflect the Statutory Obligations of the LECs.

The Commission also properly seeks comment on various issues regarding interconnection rules between CMRS carriers and LECs, particularly RLECs, as it is important to resolve these issues within the comprehensive scope of all intercarrier compensation issues. These issues must be resolved in compliance with the statute provisions requiring LECs to interconnect *within their networks* and requiring LECs to provide equal access. The over-reaching demands of some CMRS providers have created interconnection chaos — disadvantaging both LECs and long-distance providers.

1. *The Commission Should Eliminate the IntraMTA Rule.*

In the *Local Competition Order*, the Commission adopted its intraMTA rule, which states that traffic to or from a CMRS network that originates and terminates within the same Major Trading Area ("MTA") is subject to reciprocal compensation obligations under section 251(b)(5) rather than interstate or intrastate access charges. The Commission concluded that the MTA is the most appropriate local service area definition for CMRS traffic for purposes of reciprocal compensation under section 251(b)(5) because artificial distinctions between CMRS providers are avoided.²⁵⁷

In the *FNPRM*, the Commission seeks comments on whether it should eliminate the intraMTA rule given the Commission's goal of moving toward a more unified

²⁵⁷ See *Local Competition Order* at ¶ 1036.

regime.²⁵⁸ The Rural Alliance believes that the intraMTA rule creates artificial distinctions between calls, confusion among carriers and regulators, and results in an inconsistent application of reciprocal compensation and access charges. The environment created by the intraMTA rule is incompatible with the Commission's goal of moving toward a more unified regime; therefore, the rule should be eliminated.

The Commission also seeks comment on how parties should determine which LEC-CMRS calls are subject to reciprocal compensation in the absence of the IntraMTA rule.²⁵⁹ In the absence of the intraMTA rule, the determination of which LEC-CMRS calls are subject to reciprocal compensation and which calls are subject to access charges should be based upon the facilities and carriers used to complete the call. Calls originated on the LEC network that terminate to an NPA-NXX rated to the rate center in which the call originated *and* routed to a CMRS carrier through a POI located within the local calling area should be subject to reciprocal compensation. The wireline local calling area or local exchange is the appropriate geographic scope for LEC-originated reciprocal compensation calls as long as the exchange of traffic and the POI is within the LEC's local exchange. Calls originated on the CMRS network and delivered directly to the LEC without an intervening IXC should also be subject to reciprocal compensation regardless of a call's point of origin. The Act's toll dialing parity obligations and the Commission's toll dialing parity rules,²⁶⁰ both require that calls utilizing facilities outside of a LEC's local exchange (i.e., interexchange facilities) should continue to be routed to

²⁵⁸ See *FNPRM* at ¶ 136.

²⁵⁹ *Ibid.*

²⁶⁰ 47 C.F.R. § 51.209.

an IXC and should continue to be subject to the access charge regime. Likewise, CMRS-originated calls terminated to a LEC by an IXC should also be subject to access charges.

This proposed methodology to determine the appropriate compensation regime, which depends upon the POI's location and whether an IXC is used to originate or complete the call, should be used no matter the type of carrier involved. If two local carriers handle a call without the use of an IXC, then reciprocal compensation applies, but if an IXC is involved in delivering the call, then access charges apply.

The Commission also asks whether intraMTA calls dialed on a one-plus basis and destined to a CMRS carrier's network can be routed to a CMRS carrier rather than to an IXC.²⁶¹ The simple response to the Commission's inquiry is "no." Once a subscriber dials a call on a one-plus basis, the end office queries its PIC table to determine the appropriate trunk for routing. The PIC information is forwarded to the tandem switch, whereby the tandem switch routes the call to the IXC pre-selected by the subscriber.²⁶² Prior to its PIC table inquiry, the end office switch can determine neither whether the call is destined to a CMRS network nor whether the call is intraMTA or interMTA. Thus, routing of one-plus dialed CMRS calls directly to CMRS carriers is impossible.

The Commission recognizes that its current rules require calls dialed on a one-plus basis to be routed automatically to the customer's pre-subscribed IXC.²⁶³ Specifically, section 51.209 of the Commission's rules requires LECs to implement toll

²⁶¹ *Ibid.*

²⁶² In the alternative, an IXC can order direct trunks to an end office. In this case, the switch routes the call along with the PIC information to the IXC's directly-connected trunk.

²⁶³ See *FNPRM* at ¶ 138.

dialing parity through a pre-subscription process. This rule codifies the requirement contained in section 251(b)(3) of the Act. As such, section 51.209 of the Commission's rules cannot be changed without a change in law.

If the Act's toll dialing parity provision were eliminated, it would still be impossible for LECs to route intraMTA calls to CMRS carriers. The intraMTA rule is based on a CMRS customer's location at a given moment, and the originating switch cannot identify whether the called customer is currently within the MTA prior to routing the call. In addition, calls terminated to a CMRS carrier within the MTA would have to be dialed on a ten-digit basis, while calls destined for landline customers located within the MTA would need to be dialed on a one-plus ten-digit basis.

Dialing procedures dependent on the nature of the terminating carrier and the location of the called party will create incredible customer confusion. Customers would need to know three things to correctly place a call: (1) whether the called customer is currently located within the MTA, (2) if the NPA-NXX code belongs to a wireless or wireline provider and (3) whether the number has been ported between wireless and wireline networks. Obviously, it is unreasonable to expect that customers will know this information. Therefore, toll dialing parity rules must be maintained and the intraMTA rule must be eliminated.

Another option the Commission seeks comments on is whether all intraMTA calls can be made subject to reciprocal compensation without requiring LECs to alter the routing of originating traffic.²⁶⁴ Such an alternative requires that calls dialed on a one-

²⁶⁴ *Id.* at ¶ 138.

plus basis and routed to an IXC be subject to both access charges and reciprocal compensation.

Subjecting traffic to two intercarrier compensation regimes contradicts overarching objectives of this proceeding—simplifying the intercarrier compensation system and treating all traffic utilizing the public network in an equitable manner. Traffic is either subject to exchange access or reciprocal compensation, depending on who is the RSP and the method of connection to the customer. In those instances where IXC traffic is terminated within an MTA to a CMRS carrier, the proper intercarrier treatment is for the CMRS carrier to bill the IXC for terminating access. This methodology is consistent with an existing Commission finding on the matter. Furthermore, applying consistent treatment of all carriers via a unified compensation regime dictates that an IXC should pay terminating access charges when it terminates a call to a CMRS provider, just as it does when it terminates traffic to a LEC. CMRS providers must be permitted to bill terminating access charges when they terminate IXC calls.²⁶⁵

2. *States Should Establish Uniform Terms for CMRS-RLEC Interconnection.*

In the *FNPRM*, the Commission recognizes that a formal negotiation and arbitration process between RLECs and CMRS providers could impose significant

²⁶⁵ The Commission found that Sprint PCS was not prohibited from seeking to assess access charges from AT&T for termination of AT&T's long distance traffic. Sprint could impose these charges unilaterally through one of three ways: 1) Commission rule; 2) tariff; or 3) contract. There are no Commission rules allowing such unilateral imposition of access charges. Additionally, CMRS carriers are subject to mandatory detariffing. Therefore, only contractual agreement is available to Sprint to justify access charge assessment on AT&T. The Commission believed it was possible for an agreement to exist without an express contract but felt that the decision was more appropriately made by a court. The Commission chose to defer judgement on other issues pending a court decision on contractual issue. *See In the Matter of Petitions of Sprint PCS and AT&T Corp. For Declaratory Ruling Regarding CMRS Access Charges*, CC Docket No. 01-316, Declaratory Ruling, FCC 02-203 (rel. Jul 03, 2002).

burdens on the parties.²⁶⁶ Therefore, the Commission seeks comments on what measures it might adopt to reduce those costs.

One way to reduce the costs of the negotiation and arbitration process is for the Commission to authorize States to establish uniform terms or master agreements for interconnection between CMRS providers and RLECs within the State. State commissions would continue to determine whether an RLEC's rates comply with the additional cost standard. Once an RLEC files its costs and the State commission determines that the costs submitted comply with the additional cost standard, the State commission would authorize the RLEC to apply the unified rate to all originating or terminating traffic. Consolidating an RLEC's cost showing into one State proceeding and establishing one master agreement per RLEC for all traffic would be more efficient than multiple LECs negotiating and arbitrating with multiple CMRS providers.

The filed rates will conform to the additional cost standard set forth in section 252(d)(2) of the Act. With respect to tariffs filed by the National Exchange Carrier Association ("NECA"), sufficient rate banding will be necessary to minimize the differences between an individual rural ILEC's rates for interconnection and its appropriate unit cost. Since parties can intervene in the tariff approval process, all parties, including those with section 251 obligations, retain due process rights. Furthermore, as required by the Act, carriers still will be able to negotiate or arbitrate these rate levels if they determine negotiations or arbitrations to be beneficial; however, modifications of the approved tariff rates should be the exception, not the norm. This process creates rates that are consistent with the additional cost standard, provides due

²⁶⁶ *FNPRM* at ¶ 140.

process for all parties, and utilizes regulatory resources efficiently by eliminating costly arbitrations.

3. *Calls Should Not Be Locally Rated and Separately Routed to a POI Beyond the Exchange.*

In the *FNPRM*, the Commission asks various questions regarding the proper routing and rating of calls. The Commission asserts that an originating LEC can “change its switch translations so a call to an NPA-NXX assigned to a rate center that is local to the originating rate center must be dialed on a one-plus basis and rated as a toll call.”²⁶⁷ The Commission further asserts that a LEC may have an incentive to engage in this practice for a variety of reasons, including increased access revenues, reduced reciprocal compensation payments and less significant transport obligations.

The Commission also asserts that standard industry practice is to look at a call’s NPA-NXX to determine how the call should be rated, and then route the call accordingly.²⁶⁸ In fact, industry practice is just the opposite. The determination of whether a call is local or toll is based on the facilities used for routing and completing the call. If a call must use interexchange facilities — facilities beyond a LEC’s local exchange or local calling area facilities — in order for its completion, such a call is properly treated as a telephone toll service call and should be rated as a toll call.

The Commission’s assertion regarding standard practice in rating and routing is incorrect and ignores standard practice as it relates to the Local Exchange Routing Guide (“LERG”) and other non-LERG routing arrangements. The LERG has historically been

²⁶⁷ *FNPRM* at ¶ 142.

²⁶⁸ *Id.* at ¶ 141.

used to identify *existing* routing arrangements for interexchange traffic and for local tandem traffic. NPA-NXX codes for all carriers are entered in the LERG showing vertical and horizontal coordinates and other information associated with the switch, such as office functionality and homing arrangements identifying the types of tandems on which an end office homes.²⁶⁹ Other non-toll routing such as EAS arrangements and local interconnection arrangements are established by mutual agreement of the companies involved and are not identified in the LERG. The purpose of the LERG is to record *existing* routing arrangements; it should not be used to create *new* routing arrangements beyond what has been negotiated today.

The controversy over rating and routing of CMRS traffic has arisen solely as a result of some CMRS carriers' deceptive misuse of the LERG in an attempt to unilaterally dictate POI locations, redefine distant toll tandems as local tandems, and shift costs to the RLEC and its customers. The *FNPRM* implies that RLECs' reaction to CMRS carriers' demands for rating and routing is outside of industry standard practice,²⁷⁰

²⁶⁹ There are currently ten possible tandems an office can home on depending on the office's function in the network and shown in the LERG, including Feature Group B, Feature Group C, Feature Group D, Operator Service, Feature Group B Intermediate, Feature Group C Intermediate, Feature Group D Intermediate, Local, IntraLATA and CS Data TDM. The LERG indicates the routing of traffic to tandems, both toll and local. In large metropolitan areas multiple end offices commonly home on a local tandem, which switches local calls among the subtending local offices. The LERG clearly describes these existing routing arrangements, identifying the switch with local tandem functionality and each office that homes on the tandem. In this situation, a wireless carrier may acquire an NPA-NXX with the same rating location as one of the ILEC's end offices. The CMRS switch would home on the ILEC's local tandem and would receive seven-digit local calling to and from all the end offices (both ILEC and CMRS) subtending the local tandem. In contrast, LERG data for a typical RLEC end office shows homing arrangements to a toll tandem, which is usually listed as being a Feature Group D, Operator Service and IntraLATA tandem. Unlike the switching configurations for metropolitan areas, RLEC end offices rarely home on a local tandem. Furthermore, the Feature Group D and Operator Service tandem on which the RLEC end office homes is designated as a toll tandem only, not a local tandem.

²⁷⁰ See *FNPRM* at ¶ 142.

but RLECs are in conformance with standard industry practice.²⁷¹ Instead, it is the CMRS carriers' demand for an unprecedented, nonsensical dichotomy (rate local, but route to a distant toll tandem) that is outside of standard industry practice.

Some CMRS carriers have surreptitiously added NPA-NXX codes to the LERG, without having first negotiated meet points or local interconnection as required by section 251. Industry standard practice is to first negotiate interconnection meet points and routing, then update the LERG to accurately reflect the negotiated arrangements. Some unscrupulous CMRS carriers have created a new form of "squatter's rights" by inappropriately and illegally reversing the process. These companies first create a LERG entry and then claim the LERG entry creates an obligation for the RLEC — an obligation that was not agreed to under negotiations pursuant to section 251. The LERG should not be used to unilaterally dictate interconnection terms nor should the LERG be used to circumvent negotiation of local routing arrangements. Yet this is how some CMRS carriers are misusing the LERG.

The telecommunications industry has wasted millions of dollars arbitrating and litigating this issue — millions that could have been used deploying broadband or improving wireless coverage. The Commission must clarify its rules to reaffirm industry standards and comport with the law by declaring the following: (1) a CMRS carrier cannot use the LERG to unilaterally dictate routing for a carrier other than itself; (2)

²⁷¹ The Commission should recognize that, as a practical matter, an RLECs' facilities often do not extend beyond its local exchange area under which it has authority to provide telephone exchange service and almost never extend to the LATA tandem, which is usually owned and operated by an RBOC, where CMRS carriers are demanding the local traffic be delivered. Thus, when calls are routed to and exchanged at a physical location outside of a RLEC exchange, such calls are routed over an interexchange facility to an IXC that provides telephone toll service to the end user originating the call. Thus, it is standard industry practice for LECs to analyze the NPA-NXX code of the LERG entry to determine where the LEC must physically route the call and the proper routing of a call ultimately determines the proper rating of a call.

CMRS carriers are required to establish local interconnection, including designating a POI, through negotiation, not through changing the LERG; and (3) if there is not a contractually established *local* POI, toll dialing parity obligations necessitate that traffic be routed over interexchange facilities to an IXC and should not be locally rated.

The Commission appropriately recognizes that the retail rating of intrastate calls and the definition of local calling areas is under the purview of State commissions. There is simply nothing ambiguous about the applicable jurisdiction of a local calling area or an intrastate call. The Commission thus questions whether it is necessary to preempt State commissions in order to consistently resolve these issues.²⁷² As described in Section V. of these Comments, the Rural Alliance does not support preemption.

D. Customers, Including Exchange Access Customers, Benefit from the Continuation of Pooling.

In the *FNPRM*, the Commission seeks comments on how to reconcile the interstate tariff process governing the access charge regime with the negotiation provisions applicable under sections 251 and 252.²⁷³ The Commission also questions the feasibility of pooling for rural companies in a new intercarrier compensation regime, particularly if the new regime is based on negotiated interconnection agreements.

The Rural Alliance supports continuation of pooling for cost recovery and the filing of a uniform common tariff because such an approach is administratively and economically efficient. A common tariff will also provide for more stable, uniform rates.

²⁷² See *FNPRM* at ¶ 143.

²⁷³ *Id.* at ¶ 116.

Under a unified regime, the existing pooling and tariffing functions can simply be expanded to include intrastate costs. The Commission has previously noted that an access plan including a unified tariff for some rate elements would produce a common tariff for a large number of rural companies with comparable costs, and would therefore promote economic efficiency.²⁷⁴

Many rural companies participate in today's pooling mechanism because of its administrative benefits. The Commission has previously recognized the administrative benefits of pooling when the pool was established in 1984:

Such voluntary arrangements not only do not have disadvantages that would warrant a prohibition, but also have important advantages. The telephone industry is composed of a limited number of large companies that serve over 90% of the local exchange subscribers and a very large number of small companies that serve the remaining subscribers. Most of these smaller companies have never filed any tariff of any kind with this Commission. It would be totally unrealistic to expect such companies to prepare and justify separate tariffs in accordance with the rules we are adopting in this *Report and Order*. It would also be unrealistic to suppose that this Commission could review 1500 access tariffs in the meaningful manner if they did choose to do so. A common tariff arrangement that most of the exchange carriers can use is clearly necessary to make any access charge rules work.²⁷⁵

The Commission appropriately acknowledged that “[w]e cannot and should not expect a telephone company with eight employees to do everything that Pacific Telephone is expected to do.”²⁷⁶ Many rural companies simply do not have the resources to develop and file individual tariffs at the Commission, nor do these companies have the

²⁷⁴ *Federal Register*, Vol. 48, No. 49, March 11, 1983, Rules and Regulations, CC Docket 78-72; FCC 82-579; Access Charges; MTS and WATS Market Structure; Final Rules at ¶ 329.

²⁷⁵ *Id.* at ¶ 337.

²⁷⁶ *Id.* at ¶ 362.

resources to negotiate and arbitrate with hundred of carriers. The Rural Alliance contends that the public policy benefits of uniform rates, terms and conditions provided by a uniform tariff are just as valid today as they were when the pool was established. The administrative streamlining that pooling creates is consistent with NARUC's principle that a compensation system should be simple and inexpensive to administer.²⁷⁷

Pooling also benefits both exchange access and end-user customers by stabilizing rates and making those rates more uniform nationally. IXCs benefit from interstate pooling because interstate rates are more uniform across the nation than those rates would otherwise be. Since the uniform tariff rates makes retail rate averaging easier, end user customers also benefit by more uniform retail toll rates. As the National Telecommunications Cooperative Association ("NTCA") correctly observed, pooling provides financial stability for rural companies, as well as administrative efficiencies not achievable on their own.²⁷⁸ Pooling reduces the risk to any one company by stabilizing cash flow and offsetting the effect of unexpected cost increases or demand reductions.²⁷⁹ Thus end-user and wholesale rate fluctuations can be avoided in compliance with NARUC's rate shock principle.²⁸⁰ By ensuring that companies earn an adequate return on their investments, pooling is also critical to a company's ability to secure capital necessary to maintain and upgrade infrastructure.

²⁷⁷ See *NARUC Principles* III. G.: "Any intercarrier compensation system should be simple and inexpensive to administer."

²⁷⁸ See *NTCA Ex Parte filing: "Bill and Keep: Is It Right for Rural America?"* CC Docket No 01-92, ("NTCA White Paper") (filed Mar. 10, 2004) at p. 35.

²⁷⁹ Unexpected demand reductions could be a result of a natural disaster or loss of a large customer.

The Rural Alliance believes that a uniform tariff will provide a forum for carriers to challenge rates, if necessary, without placing unfair and costly administrative burdens on rural companies.²⁸¹ Protracted litigation can result from inconsistent and ill-defined interconnection rules, as evidenced by the recent T-Mobile petition.²⁸² This litigation serves an example of how RLECs can be disadvantaged when larger carriers refuse to negotiate or recognize rural cost differences.

The pooling and uniform tariff mechanism has worked well for over twenty years because it allows for consistent, even-handed application of rates, terms and conditions without placing an unfair burden on any individual carrier. If consistent rules, similar to those applied to IXC's, were applied uniformly to all wholesale providers, then only minor network changes would be needed today. For the above reasons, the Rural Alliance cannot support any mandate that would require over a thousand NECA members to abandon the uniform tariff and pooling process in favor of one process that would require direct negotiations with hundreds of carriers.

²⁸⁰ See *NARUC Principles* VII. A.: "The transition to a new intercarrier compensation system should ensure continuity of existing services and prevent significant rate shock to end-users. Penetration rates for basic service should not be jeopardized."

²⁸¹ The Rural Alliance recognizes the tariff flexibility rules that are in place today via Commission orders and rules and is not recommending that those rules be changed. The Rural Alliance recommends that companies that voluntarily file their own tariffs be allowed to continue.

²⁸² See *In the Matter of Developing a Unified Intercarrier Compensation Regime*, CC Docket 01-92 and *T-Mobile et al. Petition for Declaratory Ruling Regarding Incumbent LEC Wireless Termination Tariffs*, CC Docket No. 01-92, Declaratory Ruling and Report and Order, FCC 05-42 (rel. Feb. 24, 2005).

V. ANY INTERCARRIER COMPENSATION REFORM MUST INVOLVE BOTH STATE AND FEDERAL REGULATORS TO BE LEGAL.

Of central importance to *any* decisions that come forth on intercarrier compensation reform are the jurisdictional issues between the Commission and the States, including whether and how issues are to be referred to Federal-State Joint Boards. The Commission addresses these unavoidable jurisdictional issues²⁸³ and seeks comment on the State preemption legal theory posited by ICF,²⁸⁴ as well as joint board referral recommendations made by the Alliance for Rational Intercarrier Compensation (“ARIC”) and the CBICC.²⁸⁵ The Commission wisely recognizes the significance of thoughtful handling of jurisdictional issues, as these are potentially among the most contentious. The Rural Alliance believes that the most practical, and legally sustainable, approach is to avoid pre-empting States’ statutory rights.

The Rural Alliance addresses the Commission’s questions about its authority to assert jurisdiction over intrastate access charges, which the Commission admits “have been an area within the exclusive jurisdiction of State commissions. ...”²⁸⁶ That passage speaks for itself, and the Rural Alliance believes the Commission should not preempt the States on intrastate access charges or, for that matter, on the review and approval of

²⁸³ See *FNPRM* at ¶¶ 78-82.

²⁸⁴ *Id.* at ¶ 82.

²⁸⁵ *Id.* at ¶ 81.

²⁸⁶ *Id.* at ¶ 78.

reciprocal compensation rates in interconnection agreements.²⁸⁷ Fortunately, the opportunity exists for the Commission and States to engage lawfully, thoroughly and expeditiously in processes to reform intercarrier compensation and establish cost-recovery alternatives necessary to preserve universal service. NARUC shares the viewpoint that Federal and State collaboration is necessary to reform the system, yet recognize State commissions' responsibilities to consumers in their States.²⁸⁸

A. Rate Unification Should Result from a State and Federal Collaborative Process.

The Commission recognizes correctly in the *FNPRM* the limitations it faces in any attempt to assert section 251(b)(5) jurisdiction over access traffic,²⁸⁹ and specifically over intrastate access, which the Commission found in its *Local Competition Order* is also “carved out” under section 251(g).²⁹⁰ The existence of this access “carve out” – coupled with State commissions' specific responsibilities for reciprocal compensation rates under section 251(b) and (d) – leaves much of the responsibility for setting

²⁸⁷ 47 U.S.C. §§ 252(a)-(c), establishing the state approval and arbitration process, and 47 U.S.C. § 252(d)(2)(A), establishing terms for a state's review of transport and termination costs.

²⁸⁸ See *NARUC Principles*:

- VI.A. The reciprocal compensation system should ensure that revenues, cost assignment, and the risk of confiscation are jurisdictionally consistent for all classes of traffic.
- VI.B. State commissions should continue to have a significant role in establishing rates and protecting and communicating with consumers.
- VI.D. State commissions should retain a role in this process reflecting their unique insights, as well as substantial discretion in developing retail rates for services provided by providers of last resort, whether a dual or unified compensation solution is adopted.
- VI.E. A proposal preserving a significant State role that fits within the confines of existing law is preferable.
- IX.E. Even when a referral to a Joint Board is not mandated by law, in order to ensure State input the FCC should make a referral, and the Joint Board should act on that referral, in an expedited manner. Similarly, referrals to Joint Conferences should be handled on an expedited basis.

²⁸⁹ 47 U.S.C. § 251(g).

²⁹⁰ See *Local Competition Order* at ¶ 732.

intercarrier compensation rates squarely in the States' hands. The plain language of the law leaves no doubt that intrastate access and reciprocal compensation prices are State commission matters. The task of unifying intercarrier compensation rates thus must be collaborative and meaningfully compliant with the spirit, intent and reality of the Act. For the Commission to pursue any other path in reforming intercarrier compensation would be counter-productive, induce numerous legal challenges and not be helpful for an industry already under duress. The Rural Alliance supports the objective of establishing a unified intercarrier compensation plan using a collaborative approach, within the framework of the Commission's existing statutory authority.

The record in this proceeding includes various proposals recommending that each company unify all intercarrier compensation rates — interstate access, intrastate access and reciprocal compensation — using a collaborative approach between State and Federal regulators. Plans recommending unification of intercarrier compensation rates through a collaborative approach include those filed by EPG, ARIC, CBICC, NARUC and NASUCA. None of these plans recommend bill and keep, except in instances when carriers voluntarily agree to such an arrangement and locally exchanged traffic is in balance, as called for under the Act.²⁹¹ The sponsors of these plans — representing a cross-section of entities with varying interests including State regulators, consumer advocacy agencies, CETCs, and mid-size and small LECs — agree that intercarrier compensation rates should be maintained as a vital cost recovery element. There is also

²⁹¹ Section 252(d)(2)(B) states that “This paragraph shall not be construed – i) to preclude arrangements that afford the *mutual recovery* of costs through the offsetting of reciprocal obligations, including arrangements that waive mutual recover (such as bill-and-keep arrangements.)” 47 U.S.C. §§ 252(d)(2)(B) and 252(d)(2)(B)(i).

agreement that each company's rates should be unified to address the arbitrage problems plaguing the industry.

B. The Industry Will Not Benefit by Preempting Intrastate Rates.

Any attempt to impose blanket preemption of State authority, in the absence of clear statutory authority, will produce huge uncertainty in an industry sorely in need of stability. Until the courts fully addressed the legal challenges that would inevitably arise, the industry would be left floundering. Those proposals set forth in this proceeding that promote Commission preemption of State authority over intrastate access raise serious questions of policy and law, as reflected by the *FNPRM*.²⁹² As a matter of policy and law, the role of the State regulator should not be overlooked or ignored. Accordingly, the Rural Alliance believes that neither the industry nor customers would benefit by a Commission attempt to pre-empt the States' statutory rights and duties over intrastate access rates and reciprocal compensation. A more prudent approach would be to involve both Federal and State regulators. Relevant statutory provisions and associated legislative history bear this out.

1. *Historically the Commission Has Lost Cases in which It Attempted to Exercise Preemption.*

Section 2 of the Act specifically states that "nothing in this Act shall be construed to apply or to give the Commission jurisdiction with respect to (1) charges, classifications, practices, services, facilities, or regulations for or in connection with intrastate communication service by wire or radio of any carrier engaged . . ." ²⁹³ While

²⁹² See, e.g., *FNPRM* at ¶¶ 63-86.

²⁹³ 47 U.S.C. § 2.

there are exceptions to this requirement, the exceptions are specific.²⁹⁴ Congress has demonstrated time and again that it knows how to amend section 152 of the Act to broaden the Commission's jurisdiction *when it elects to do so*.

Any Commission attempt to set intrastate rates would be tantamount to asserting jurisdiction over intrastate access or reciprocal compensation. As the Fifth Circuit Court of Appeals found, the Commission is prohibited from taking any action to assert jurisdiction over intrastate matters without a finding that section 254 of the Act applies.²⁹⁵ No such finding exists. Indeed, the opposite is true as evidenced by the Commission losing *TOPUC I*. Commission attempts to set intrastate rates would encourage litigation and create more instability.

Another example of the Commission failing in its attempt preempt the States was in Louisiana Public Service Commission et al. v. Federal Communications Commission, (the "*Louisiana Decision*"). The Court considered and rejected the Commission's attempt to preempt the States on the establishment of State depreciation rates of common carriers. The Court determined that preemption is not lawful where it is not based on statutory authority. The Court considered and fully rejected the argument that the Commission should be able to preempt State authority in order to foster Federal policy:

While it is certainly true, and a basic underpinning of our Federal system, that State regulation will be displaced to the extent that it stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress, Hines, 312 U.S., at 67, 61 S.Ct., at 404, it is also true that *a Federal agency may pre-empt State law only when and if it is acting within the scope of its congressionally delegated authority*. This is true for at least two reasons. First, an agency literally has no power to act,

²⁹⁴ 47 U.S.C. §§ 223 – 227.

²⁹⁵ See Texas Office of the Public Utilities Counsel v. FCC, 183 F.3d 393, ("*TOPUC I*") (5th Cir. 1999).

let alone pre-empt the validly enacted legislation of a sovereign State, unless and until Congress confers power upon it. Second, the best way of determining whether Congress intended the regulations of an administrative agency to displace State law is to examine the nature and scope of the authority granted by Congress to the agency. Section 152(b) constitutes, as we have explained above, a congressional *denial* of power to the FCC to require State commissions to follow FCC depreciation practices for intrastate ratemaking purposes. *Thus, we simply cannot accept an argument that the FCC may nevertheless take action which it thinks will best effectuate a Federal policy.* An agency may not confer power upon itself. To permit an agency to expand its power in the face of a congressional limitation on its jurisdiction would be to grant to the agency power to override Congress. This we are both unwilling and unable to do.²⁹⁶

Even though the Act does not specifically confer power on the Commission to preempt States from establishing intrastate access charges, the *FNPRM* seeks comment on whether the Commission can assert preemptive rights based on several specific statutory provisions or the alternative “mixed use doctrine.”²⁹⁷ None of these considerations, however, can lend unambiguous support to a claim of preemptive authority over the States for the establishment of intrastate access charges.

2. Section 251(b)(5) Is Not Applicable to All Telecommunications Traffic.

In the *FNPRM*, the Commission states that “on its face” section 251(b)(5) applies to all telecommunications.²⁹⁸ This presumption is incorrect. The error is borne out both by the legislative history of the Act and by subsequent Court decisions.

Section 251(b) was established to set forth specific interconnection requirements applicable to LECs in the context of the development of competitive local markets.

²⁹⁶ See *Louisiana Decision* at pp. 374-375, emphasis added.

²⁹⁷ *FNPRM* at ¶ 80.

²⁹⁸ *Id.* at ¶ 90.

Section 251(b)(5) specifically addresses the duty of LECs to transport and terminate traffic of other LECs who compete in the same local exchange service area. Section 251(b)(5) has absolutely nothing to do with the provision of interstate or intrastate exchange access services. LECs simply do not have “reciprocal compensation arrangements” with IXCs.²⁹⁹ In fact, Congress specifically distinguished exchange access services from reciprocal compensation transport and termination arrangement required pursuant to section 251(b)(5). Congress acted to ensure that new competitive local exchange service providers could utilize the facilities and equipment of incumbent local exchange carriers “for the transmission and routing of telephone exchange service *and exchange access.*”³⁰⁰

In addition, section 251(b) simply does not apply to “all telecommunications.” The legislative history reveals that the plain words of the Act are consistent with the Congress’ intent. Both the Senate and the House considered legislation to promote a competitive local exchange market. The Senate bill established a new section 251 to impose duties on local exchange carriers “to negotiate in good faith and to provide interconnection with other telecommunications carriers that have requested interconnection for the purpose of providing telephone exchange service or exchange access service.”³⁰¹ Most significantly, the legislative history of the Senate bill states:

²⁹⁹ The fact that a local exchange carrier may also have an IXC “affiliate” does not give rise to a right for the IXC affiliate to seek “reciprocal compensation” of its interexchange traffic that is subject to access charges.

³⁰⁰ 47 U.S.C. § 251(c)(2)(A), emphasis added. The Rural Alliance notes that Rural Telephone Companies are exempt from this requirement pursuant to § 251(f)(1)(A) of the Act. *See also* 47 U.S.C. § 251(f)(1)(A).

³⁰¹ H.R. CONF. REP. 104-458 at p. 117.

The obligations and procedures prescribed in this section do not apply to interconnection arrangements between local exchange carriers and telecommunications carriers under section 201 of the Communications Act for the purpose of providing interexchange service, *and nothing in this section is intended to affect the Commission's access charge rules.*³⁰²

The legislative history further indicates that the House and Senate Conference reached agreement that “adopts a new model for interconnection that incorporates provisions from both the Senate bill and House amendment in a new section 251 of the Communications Act.”³⁰³ Neither the words of the Act, nor the legislative history, nor the interpretation of section 251(b)(5) by the Courts³⁰⁴ or the Commission itself suggest any basis to conclude that section 251(b)(5) has anything to do with access charges. To the contrary, the legislative history specifically indicates the opposite intent. Section 251(b)(5) provides no basis for the Commission to preempt State jurisdiction over intrastate access charges.

3. Section 251(g) Does Not Give the Commission Authority over Intrastate Access.

The *FNPRM* suggests that section 251(g) of the Act gives the Commission authority to preempt State jurisdiction over intrastate access charges.³⁰⁵ In support of this possibility, the Commission cites its own decision in the *Local Competition Order*, where

³⁰² *Id.* emphasis added.

³⁰³ *Id.*, at p. 123.

³⁰⁴ See, *TOPUC I* at p.424. The Court of Appeals distinguishes the applicability of § 254 of the Act from § 251 and § 252, stating, “Unlike §§ 251 and 252, which were solely concerned with intrastate issues (i.e., interconnection of new entrants into the local telephone market), § 254 applies to both interstate and intrastate services.”

³⁰⁵ *FNPRM* at ¶ 79.

the Commission found that the section 251(g) carve-out includes intrastate access services.³⁰⁶ This reasoning, however, is inapposite.

The referenced portion of the *Local Competition Order* did not support a contention that the Commission has Congressional authority to supersede State jurisdiction over intrastate access charges. To the contrary, the Commission recognized that it has no such jurisdiction, and thus no basis to disrupt intrastate access charge ratemaking:

Moreover, although section 251(g) does not directly refer to intrastate access charge mechanisms, it would be incongruous to conclude that Congress was concerned about the effects of potential disruption to the interstate access charge system, but had no such concerns about the effects on analogous intrastate mechanisms.³⁰⁷

The plain words of section 251(g), in fact, have nothing to do with establishing Commission authority to change the access charge mechanism. The Commission has always had the authority to establish the terms and conditions for interstate access, but it never has had authority to impose terms and conditions on intrastate access. The enactment of section 251(g) changed nothing in this regard. To the extent that section 251(g) addresses the continuation of terms and conditions pursuant to the provision of interstate exchange access, this section of the Act is consistent with the intent of both the Senate bill and legislative history: “*Nothing in this section is intended to affect the Commission’s access charge rules.*”³⁰⁸

³⁰⁶ *Ibid.*

³⁰⁷ See *Local Competition Order* at ¶ 732.

³⁰⁸ *Id.* emphasis added.

The inclusion of section 251(g) in the Act, however, was intended by Congress to do far more than to tell the Commission that section 251 was not established to affect the access charge rules. As the plain words of section 251(g) demonstrate, the focus of Congress in this section was to clarify the intent that the RBOCs and GTE not be permitted to utilize the prospective termination of the AT&T Consent Decree as an excuse to stop providing “equal access and nondiscrimination to interexchange carriers and information service providers.”³⁰⁹ The legislative history is clear in this regard:

The approach of both the Senate bill and the House amendment assumed that Bell Operating Companies (“RBOCs”) would be required to continue to provide equal access and nondiscrimination to interexchange carriers and information service providers under those parts of the AT&T Consent Decree that would have remained in effect under either approach. Because the new approach completely eliminates the prospective effect of the AT&T Consent Decree, some provision is necessary to keep these requirements in place. By the same token, although not specifically addressed in either the Senate bill or the House amendment, some provision is also needed to ensure that the GTE Operating Companies that provide local exchange services continue to provide equal access and nondiscrimination to interexchange carriers and information service providers.

Accordingly, the conference agreement includes a new section 251(g). . . . *When the Commission promulgates its new regulations, the conferees expect that the Commission will explicitly identify those parts of the interim restrictions and obligations that it is superseding so that there is no confusion as to what restrictions and obligations remain in effect. These interim restrictions and obligations shall be enforceable in the same manner as Commission regulations.*³¹⁰

The additional authority granted to the Commission by section 251(g) has nothing to do with authority over access charges. The Commission already had authority over interstate access charges and did not require the enactment of section 251(g) to confer

³⁰⁹ H.R. CONF. REP. 104-458 at p. 122.

³¹⁰ *Id.* at pp. 122-123.

power to change its access charge rules. As reflected by both the plain words of section 251(g) and the legislative history quoted above, section 251(g) gave the Commission the authority to continue enforcement of certain requirements and obligations imposed on the RBOCs and GTE that might otherwise have expired with passage of the 1996 Act. Section 251(g) did not give the Commission authority to preempt the State jurisdiction over intrastate access charges.

4. *Section 254(g) Does Not Give the Commission Authority over Intrastate Access.*

The *FNPRM* invites comment on whether the section 254(g) requirements for geographic rate averaging and integration lend support to a conclusion that preemption is necessary.³¹¹ While the Rural Alliance has recognized these concerns, as demonstrated by the proposals of both ARIC and EPG, the Rural Alliance respectfully submits that section 254(g) does not provide a basis to preempt State authority over intrastate access charges.

The Rural Alliance is well aware that minimizing the disparity between the access rates of price cap and rate-of-return carriers is necessary. The Commission has recognized that existing rate disparities “may create pressure on interexchange carriers to deaverage long distance toll rates,” and more consistency among rate levels is required to “promote the toll rate averaging policies codified in section 254(g).”³¹² The Rural Alliance agrees that rate changes are necessary, such as were proposed in the ARIC and EPG plans. But to suggest that rate changes are required to ensure that rural consumers benefit from section 254(g) is nonsensical and ignores the intent of the law.

³¹¹ *FNPRM* at ¶¶ 63 and 83-89.

³¹² *MAG Order* at ¶ 64.

Congress understood that access cost disparities exist and thus there will be rate disparities between larger urban-based LECs and RLECs. In fact, the principal reason for the inclusion of geographically averaged rates in the 1996 Act was to handle this issue, and thus requires IXC's to do so.³¹³ The statute does not require the entire RLEC industry to establish access charges and structures replicating those of the larger LECs. Larger LECs serve markets where they can avail themselves of scale economies, whereas smaller LECs serve markets where the costs are higher and scale economies are not possible. The statutory expectation was that when IXC's fulfilled their obligation to establish geographically averaged toll service offerings the IXC's would accommodate higher rural rates, which reflect the higher rural costs of providing interstate access service.

Congress did not expect rural access rates and structures to be changed in order that section 254(g) be adopted and enforced. To the contrary, the legislative history indicates that "the conferees do not intend that this subsection would require the renegotiation of existing contracts for the provision of telecommunications services."³¹⁴ Congress did not intend the enactment of this provision to require changes in existing arrangements. As noted above, the need for section 254(g) arises largely because of the disparate costs of access in rural and insular areas. Section 254(g) is a response to this disparity. The Commission is required to address geographic *retail* rate averaging and integration, not geographic *access* rate parity. This provision does not provide an

³¹³ 47 U.S.C. § 254(g).

³¹⁴ H.R. CONF. REP. 104-458 at p. 132

independent statutory basis to justify preemption of State jurisdiction over intrastate access charges.

5. *The “Mixed Use” Doctrine Cannot Be Used to Assert Jurisdiction over Intrastate Access.*

The *FNPRM* also seeks comment regarding whether the Commission could reform intrastate access charges by invoking the “mixed use” doctrine whereby traffic is treated as jurisdictionally interstate if it is impossible or impractical to separate the interstate and intrastate components.³¹⁵ The problem with seeking sanctuary for Commission preemption of State authority under this doctrine is that the facts inconveniently get in the way.

A long industry history exists demonstrating that it is neither impossible nor impractical to separate the interstate and intrastate usage of interexchange interconnection services. Carriers have separately identified intrastate and interstate access services since the inception of access charges. Where carriers have determined that it is either administratively or economically inefficient to separate the jurisdiction of traffic on a specific basis, mutually agreed upon imputed usage factors are applied subject to practices and procedures set forth in lawfully effective tariffs. No matter which carrier (VoIP provider, CMRS carrier or LEC) transmits the traffic, traffic factors can still be used. In fact, interconnection agreements between CMRS providers and LECs regularly establish traffic factors by mutual agreement.

While administrative and economic considerations may render it difficult for carriers to apply actual measurement, such considerations have not led to preemption of

³¹⁵ See *FNPRM* at ¶ 80.

the State jurisdiction. To the contrary, in the very instance of the application of the “mixed use doctrine” referenced by the *FNPRM*, a Joint Board was convened pursuant to section 410(c) of the Act specifically to make a recommendation on the separations procedures appropriate for mixed use special access lines. In adopting the recommendation of the Joint Board, the Commission stated:

We believe that the separations procedures recommended by the Joint Board for mixed use special access lines resolve existing concerns in a manner that reasonably recognizes State and Federal regulatory interests and fosters administrative simplicity (footnote omitted) and economic efficiency.”³¹⁶

In adopting the recommendation of the Joint Board, the Commission further emphasized that the result reflected the dual jurisdictional regulatory structure of the Act:

Based on the record in this proceeding, we agree with the Joint Board’s conclusion that the new separations procedures for mixed use special access lines are consistent with *Smith v. Illinois Bell Telephone Co.*, 282 U.S. 133 (1930), and the subsequent court decisions. (Footnote omitted). We also believe that the tariffing implications of the new separations rules (i.e., that some interstate traffic will be carried over State tariffed lines and vice versa) is in these circumstances consistent with the system of Federal and State regulation established in the Communications Act, which provides a central role for the separations process in determining the scope of state and Federal ratemaking authority. (Footnote omitted). Thus, we conclude that the proposed separations procedures properly reflect the dual jurisdictional regulatory structure of the Act.³¹⁷

The Rural Alliance respectfully submits that the “mixed use doctrine” cannot provide the basis for the Commission to preempt State jurisdiction over intrastate access charges. Instead, the Commission’s prior application of the “mixed use doctrine”

³¹⁶ See *MTS and WATS Market Structure, Amendment of Part 36 of the Commission’s Rules and Establishment of a Joint Board*, CC Docket Nos. 78-72, 80-286, Decision and Order, 4 FCC Rcd 5660 (1989) at ¶ 6.

³¹⁷ *Id.* at ¶ 7.

demonstrates the prudence of referring matters “regarding the relationship between rate structures, accounts, charges, practices, classifications, and regulations of carriers subject to the jurisdiction of such State commission and of the Commission.”³¹⁸ The Rural Alliance supports the ARIC and EPG proposals, both of which recommend that the Commission avail itself of the benefits of the collaborative Joint Board process.³¹⁹

C. A Joint Board Referral Is Necessary to Address the Impact of Intercarrier Compensation Reform.

The Rural Alliance respectfully observes that the consideration and adoption of changes in intercarrier compensation cannot be achieved in the absence of Joint Board referrals.

1. A Joint Board Referral Should Be Made to Ensure Universal Service Is Upheld.

The Rural Alliance believes that a Joint Board referrals is in order because of the linkage between access charge cost recovery and the Federal USF. Obviously, the same linkage exists between intrastate access and universal service. Some States have explicitly addressed that linkage by establishing State universal service mechanisms when reductions in access charges were effectuated. The nationwide disparity in intrastate access rates (as well as end-user rates to a large extent), and the States’ varying approaches to access reform, also makes a Universal Service Joint Board referral necessary.³²⁰

³¹⁸ 47 U.S.C. § 410(b).

³¹⁹ See *ARIC Plan* at pp. 37, and 63-65. See also *EPG Plan* at p. 28.

³²⁰ ARIC’s plan recommended that referrals be made to the Joint Board on Separations regarding unification of intercarrier compensation rates and to the Joint Board on Universal Service regarding nationwide local rate rebalancing. See *ARIC Plan* at p. 37 and pp. 63-65, respectively.

Linkage between access charges and universal service is nothing new. In the past, the Commission has recognized this relationship by “cross-docketing” access reform dockets with the universal service reform docket. Interstate and intrastate access charges and universal service funds exist to compensate eligible carriers for building and maintaining networks benefiting all customers and all service providers. As changes to intercarrier compensation are contemplated, the appropriate universal service considerations need to be made to ensure that the public network remains viable. Especially in light of heightened concerns about national security and public safety, a Joint Board referral is the proper step. Now more than ever, Federal and State regulators must cooperate to uphold universal service while intercarrier compensation modifications are under review.

2. *A Joint Board Referral Is Required to Assess the Impact on Jurisdictional Separations.*

The Commission ponders whether a mandatory referral to the Separations Federal-State Joint Board is needed pursuant to section 410(c) of the Act.³²¹ Section 410(c) specifies that the Commission is required to refer to the Joint Board “any proceeding regarding the jurisdiction separation of common carrier property and expenses between interstate and intrastate operations.”³²² Pending intercarrier compensation reforms unquestionably necessitate such a referral.

The existence of regulated cost separations indicates that there is a *need*, not to mention a *requirement*, to properly allocate costs between interstate and intrastate

³²¹ See FNPRM at ¶ 81.

³²² 47 U.S.C. § 410(c).

jurisdictions. The separations process also implies that there is an associated service in each jurisdiction that recovers those costs. Congress indeed specified in section 251(d)(3) of the Act that the preservation of intrastate access charge mechanisms was appropriate to the extent that a State commission order or regulation: (a) establishes access and interconnection obligations of LECs, (b) is consistent with the requirements of section 251, and (c) does not substantially prevent implementation of the requirements of that section and the development of competitive markets.³²³

Any changes in the *level* of intrastate access charges, which are likely as a result of this proceeding, will significantly affect cost recovery. Additionally, the creation of any new mechanisms or modifications to existing rate *structures* in an effort to offset those intrastate access changes will also force changes to existing separations allocations. Under the mandatory referral provisions of section 410(c), the Commission must refer the resulting separations implications to the body responsible for making such recommendations, the Federal-State Joint Board on Separations.

3. *A Joint Board Referral Would Be Needed to Supersede Access under Section 251(g).*

While the Rural Alliance maintains that it is entirely inappropriate for the Commission to eliminate access charges, if the Commission were to do so in the future, it must first make a referral to the Separations Joint Board. Were the Commission to only supersede interstate access charges, without similar action by the States, the result would be nonsensical: interstate access is discontinued, while intrastate access remains intact. It has been established repeatedly that the Commission does not have authority over

³²³ 47 U.S.C. § 251(d)(3).

intrastate access and thus could not supersede intrastate access charges on its own volition. Only the State commissions could supersede intrastate charges. Elimination of access without referral to a Joint Board would create the ultimate arbitrage inducement, which is among the many problems the Commission seeks to remedy.

D. The Rural Alliance Examines the Efficacy of the Major Plans.

1. *The ICF Plan Obviates the Joint Board Referral Provisions.*

The ICF states that the establishment of a bill-and-keep regime through an increase in SLCs and the replacement of interstate and intrastate switched access revenues would not require a referral to the Separations Joint Board under section 410(c).³²⁴ It argues that there is no change in the separation allocation of costs between jurisdictions and therefore, no referral is necessary.

The Rural Alliance believes the ICF is mistaken in its interpretation of the Joint Board provisions. Congress felt strongly enough about States' input into important policy and regulatory decisions that could dramatically impact States' rights and responsibilities that it enacted legislation mandating State and Federal consultation. Section 410(c) states:

The Commission shall refer any proceeding regarding the jurisdictional separation of common carrier property and expenses between interstate and intrastate operation, which it institutes pursuant to a notice of proposed rulemaking and, except as provided in section 409 of this title, may refer any other matter, relating to common carrier communications of joint Federal-State concern to a Federal State Joint Board.³²⁵

³²⁴ See *ICF Brief* at footnote 73, p.45.

³²⁵ 47 U.S.C. § 410(c).

Costs are the primary driver for compensation structures; therefore, only if there is a redistribution of costs between jurisdictions should there be a restructure of the compensation system. Obviously, moving to a bill-and-keep regime for both Federal and State access as well as reciprocal compensation involves a shifting of cost recovery. As a result of compensation changes, the Joint Board on Separations must have input into any underlying redistribution of costs. The ICF plan ignores the mandatory Joint Board on Separations referral, while proposing a massive change in compensation.

Even if the Commission finds that the mandatory referral does not apply, section 401(c) also contains permissive referral language in “any other matter, relating to common carrier communications.”³²⁶ A major shift of costs and compensation is clearly a matter relating to common carrier communications. To undertake such a radical change without Federal/State consultation and cooperation would be at odds with the intent of the law.

The ICF plan also asserts that no referral to the Universal Service Joint Board is required under section 254(a) because that board’s purpose was solely for the implementation of universal service requirements. The ICF argues that the plan does not require a change in the definition of universal service.³²⁷ The ICF plan’s claim that section 254(a) does not apply fails under scrutiny. Section 254(c) states that “[u]niversal service is an evolving level of telecommunications services...”³²⁸ The appreciation of universal service evolution is clear from the Commission’s referral of issues to the

³²⁶ *Ibid.*

³²⁷ See *ICF Brief* at footnote 73 p. 45.

³²⁸ 47 U.S.C. § 254(c)(1).

Universal Service Joint Board in 2002. The Commission, in its referral order, asked the Board to “review certain of the Commission’s rules relating to the high-cost universal service support mechanisms.[...]We request the Joint Board provide recommendations to the Commission regarding if and how those rules should be modified.”³²⁹ In this referral order, the Commission asks the Joint Board for comment and recommendations. This referral shows the Commission’s appreciation that “there have been many changes in the telecommunications marketplace”³³⁰ and that Federal-State cooperation is important to a successful transition through difficult industry growing pains.

2. *The ICF Plan Inappropriately Preempts the States’ Roles in Intercarrier Compensation.*

The ICF asserts that under the Supreme Court’s holding in AT&T Corp. v. Iowa Utilities Board,³³¹ the Commission has authority under sections 201 and 251(b)(5) to address the compensation rules applicable for the exchange of all telecommunications traffic, whether “local” or “long distance,” “interstate” or “intrastate.” Additionally, ICF asserts the Commission has broad independent authority under section 254 to prohibit mechanisms, such as traditional intrastate access charges, that represent unsustainable sources of universal service so long as the Commission ensures that those mechanisms are replaced with more durable support mechanisms.³³² The arguments proffered by the

³²⁹ *In the Matter of Federal-State Joint Board on Universal Service*, CC Docket 96-45, Order, FCC 02-307 (“Referral Order”) (rel. Nov 8, 2002) at ¶ 1.

³³⁰ *Id.* at ¶ 4.

³³¹ AT&T Corp. v. Iowa Utilities Board, 525 US 366 (1999).

³³² *See ICF Brief* at pp. 7-8.

ICF were encompassed in the questions posed by the Commission in the *FNPRM*. As a result, the Rural Alliance references the previous arguments in this section.

3. *NASUCA Correctly Maintains that States Should Retain Control over Local and Access Rates.*

The Rural Alliance agrees with NASUCA in its belief that States must retain authority over rates for services provided in the intrastate jurisdiction. The Commission should not overreach the authority granted it in Federal law, but should instead adopt a course of action that will respect the appropriate balance between Federal and State jurisdiction embodied in the Act.

4. *CBICC Correctly Proposes a Collaborative Process between State and Federal Regulators.*

CBICC agrees with the Rural Alliance that the Commission should establish a collaborative process with State regulators and should refer matters to the Federal-State Joint Board of the need to reconcile intrastate rates to a uniform rate.³³³ CBICC recognized the necessity of proper handling of jurisdictional issues with its referral to the Joint Board on issues related to intrastate access charges. Again, the Rural Alliance believes that such referral is mandated under section 410(c).

³³³ *CBICC Plan* at p. 2.

VI. THE RECORD ON INTERCARRIER COMPENSATION WILL NOT BE COMPLETE WITHOUT AN ANALYSIS OF ISP-BOUND TRAFFIC AND IP INTERCONNECTION.

The Commission's *FNPRM* focuses solely on intercarrier compensation issues and possible reforms in the circuit-switched world. The *FNPRM* is largely void of one critical component of circuit compensation that has caused significant arbitrage problems – treatment of ISPs utilizing LEC networks.³³⁴ If modifications to the Commission's Enhanced Service Provider (“ESP”) exemption are not made in concert with other circuit-based reforms, ISPs and the CLECs that serve them will continue to benefit from

³³⁴ Since an ISP does not have a physical connection to its customers, it must acquire such capability from other providers, usually LECs or cable providers. While this service would normally be subject to access charges, the Commission's ESP exemption allows the service to be exempt from access charges if the ISP purchases local lines for the initiation of dial-up Internet connections instead. It was never the intent of the ESP exemption, however, to exempt ISPs from appropriate charges for the termination of traffic to the PSTN. To offer broadband, the ISP either buys DSL access service from a LEC's special exchange access tariff or purchases a similar service from a cable provider. To both of these services the ISP adds its own routing functionality and either uses its own backbone facilities or acquires backbone services to enable its end users to reach IP addresses worldwide.

In the instance of dial access, the ISP is structurally similar to an IXC: both are Retail Service Providers, but neither owns facilities physically connected with its customers. The purchase of wholesale access services from the LEC allows the IXC to provide long-distance service. Likewise, the purchase of wholesale access services from the LEC (using the ESP exemption) allows the ISP to provide Internet access service. From a functional perspective, the LEC is providing an end-user physical connection and switching resources on a wholesale basis to both IXCs and ISPs. But for the limited dial-up ESP exemption (which the Rural Alliance does not propose to eliminate), it would be appropriate that switched exchange access would be charged in both cases. The application of exchange access is also consistent with the broadband access model whereby DSL service is offered to ISPs as an exchange access service.

The situation becomes slightly more complicated if there are multiple LECs involved. If two LEC networks are involved in a call bound to an IXC, the IXC would be billed the appropriate switched exchange access by both LECs on a multiple-tariff, multiple-bill basis. This situation also exists for calls bound for an ISP; therefore, both LECs should bill exchange access. But under the Commission's current ESP exemption, the ISP has no obligation to pay switched access for traffic originating on a LEC's network bound for an ISP over local exchange service lines.

To avoid disruption in the industry, the Rural Alliance proposes that the Commission should continue to apply the ESP exemption to the narrow cases where a LEC and an ISP are directly connected. When another LEC, usually a CLEC, provides the local exchange service to the ISP and a customer physically connected to the ILEC's network uses the ISP's dial-up Internet service, the CLEC receives payment for local service but the ILEC receives no compensation. To be properly compensated under the ESP exemption for ISP-bound traffic that traverses the ILEC's network, the ISP must either pay the ILEC exchange access charges or connect directly to the ILEC and pay local service charges. The ISP could

arbitrage, thus defeating a primary objective of the entire proceeding. In addition, the *FNPRM* devotes virtually no attention to interconnection, compensation or universal service issues in the evolving IP world.³³⁵ The Rural Alliance devotes attention to these issues in these Comments, as solutions to circuit-based intercarrier compensation issues will not be beneficial if not accompanied by comparable solutions – or at least development of a roadmap toward such solutions – in the IP environment.

A. As ISPs Handle More Traffic, Additional Requirements Are Necessary.

IP services are becoming more widespread and are putting strain on circuit-switched compensation. An ISP's services, both VoIP and terminating long-distance, are removing some of the circuit-switched compensation that traditionally has supported the network. On the originating side, VoIP is replacing traditional PSTN calling. On the terminating side, ISPs are terminating calls back to the PSTN without compensating the LEC. In addition, ISP-bound traffic has been problematic ever since CLECs learned the game of providing service to ISPs and reaping reciprocal compensation payments in the process. The Commission's stop-gap attempts to solve the reciprocal compensation problems have been repeatedly overturned in court.

Clearly, a longer-term solution is needed. Some say that the law must be changed. While that solution may be necessary in the long-run, in the short-run problems

choose to pay local service charges, in lieu of access charges, to handle originating traffic by directly connecting to each LEC that provides physical connectivity for the ISP's customers.

³³⁵ The Commission has an open docket addressing questions concerning IP regulation. *See In the Matter of IP-Enabled Service*, CC Docket No. 04-36. The Rural Alliance believes matters investigated in that proceeding must be incorporated into the instant proceeding, as circuit-switched and IP compensation and interconnection are critically interrelated.

need attention. The Rural Alliance recommends that the following measures be implemented. These recommendations represent a reasoned approach with a sound theoretical basis to handling the problems.

1. *Traffic Terminated on the PSTN through ISPs Should be Subject to Access Charges.*

Currently, IXCs needing to terminate long distance traffic contract with ISPs for terminating services. In this symbiotic relationship the IXCs can avoid access charges and CLECs use the additional terminating traffic to stay under the 3-to-1 terminating to originating ratio. Even though termination services are contracted through an ISP, the IXC still has the obligation to pay the wholesale local provider, the LEC, to terminate traffic. The Commission's ESP exemption was never intended to allow an IXC to terminate intercarrier traffic for free over local lines to the LEC's network. The Rural Alliance recommends that access charges apply to all traffic terminated from an IXC via an ISP to the PSTN no matter whether the ISP is directly or indirectly connected to a LEC network. This conclusion is entirely consistent with the AT&T VoIP Order, in which the Commission ruled that if traffic utilizes the PSTN, circuit-switched compensation should be paid.³³⁶

2. *Reciprocal Compensation Should Not Apply to ISP Traffic between ILECs and CLECs.*

The Internet end-user is the "final" customer of the ISP's Internet retail service; thus the ISP is the Retail Service Provider to the end-user who is physically connected to either the ILEC's or CLEC's network. The customer is physically connected to the

³³⁶ See *In the Matter of Petition for Declaratory Ruling that Phone-to-Phone IP Telephony Services Are Exempt from Access Charges*, WC Docket No. 02-361, Order, FCC 04-97 ("AT&T VoIP Order") (rel. April 21, 2004) at p. 11 n. 10.

ILEC's or CLEC's network and the ILEC or CLEC is the retail provider to the end-user for local service, but neither the ILEC nor the CLEC provides the *retail Internet service* to the end-user customer. As such, no reciprocal compensation obligation under section 251(b)(5) exists between the two LECs because neither LEC is providing the retail service for the Internet call to the ISP. This approach would render the classification of traffic between an ILEC and CLEC based on the 3-to-1 terminating to originating ratio irrelevant.³³⁷

3. *ISPs Should Contribute to Universal Service Funding.*

Today's underlying physical network is used for both conventional circuit switching and IP packet switching. The most costly portions of the telecommunications network, namely the local distribution and transport facilities, are the same for both platforms. The primary difference between the two platforms is in *how* information is switched and transported over these very same facilities.

ISPs use the telecommunications network to reach their end-user customers and to transport information through the network. As such, ISPs should contribute to the maintenance of the network through universal service funding, just as CMRS carriers and IXC's do. Some call universal service contributions "taxing the Internet." The Rural Alliance maintains such a stance is nonsensical. Helping to support the infrastructure that the ISPs use for their livelihood is no more "taxing the Internet" than charging rent to an

³³⁷ The Commission established this ratio to discriminate between traffic subject to reciprocal compensation and traffic not subject to reciprocal compensation. *See In the Matter of Implementation of the Local Competition Provision of the Telecommunications Act of 1996*, CC Docket No. 96-98 and *Intercarrier Compensation for ISP-Bound Traffic*, CC Docket No. 99-68, Order on Remand and Report and Order, FCC 01-131 ("ISP Remand Order") (rel. April 27, 2001) at ¶ 79.

ISP provider who rents office space. The ISP is simply helping fund the network it uses to provide its service.

4. *The Rural Alliance's Practical Approach to ISP Traffic Is both Fair and Necessary.*

The Commission's adoption of the Rural Alliance's proposal relative to the interconnection of ISPs and LEC networks would eliminate the arbitrage opportunities prevalent with the existing interconnection scenario without unduly burdening ISP customers continuing to use dial-up connections. Such a solution would also render CLEC business plans based entirely on the gaming of compensation irrelevant. Furthermore, adoption of this proposal would allow long-distance providers to compete on a level playing field where all providers that terminate traffic to the PSTN, irrespective of their classification, would be subject to the same obligations. As Internet access traffic migrates to LEC broadband access platforms, ISP-bound traffic will be increasingly handled by broadband access services. Eventually the ESP exemption, which was designed to limit the burdens placed on dial-up services, will become irrelevant. Until such time, the above proposal is both fair and necessary.

B. The Commission Should Investigate Intercarrier Compensation in the IP Environment.

1. *IP Compensation and Interconnection Should Be Part of the Intercarrier Compensation Inquiry.*

In this Notice the Commission has focused its attention on interconnection compensation issues in the context of circuit-switched telephony, but public policy questions surrounding interconnection are not confined to circuit-switched network technologies. Perhaps even more important than studying interconnection for the circuit-

switched world is studying how interconnection will be handled in the IP world, because eventually all traffic will be handled through IP. NARUC agrees that the choices made today for PSTN compensation should anticipate and complement what will happen in IP compensation.³³⁸ To not examine and address IP compensation would ignore important evidence and leave significant compensation issues unresolved. As the public network evolves from one based on circuit switching to one based on IP switching, the Commission must manage this transition to ensure that customers have choices and independent providers can compete.

The Rural Alliance recommends that the Commission examine IP interconnection compensation to complete the record in this Notice. Doing so will assist the Commission in determining whether a bill-and-keep regime should be applied to the PSTN environment and whether regulatory oversight of IP interconnection is advisable to maintain an open and robust public Internet platform. Another related issue in need of study is the cost recovery in an IP environment. Since RLECs will no longer receive substantial intercarrier compensation payments in an IP environment, there are significant high cost support funding questions that must be considered as communications applications migrate to an integrated-services IP platform.

2. *IP Interconnection Provides Insight into Bill and Keep for the Circuit-Switched Environment.*

In order to evaluate the similarities between IP and PSTN compensation it is instructive to understand the basis for IP compensation. Interconnection in the IP

³³⁸ See *NARUC Principles VIII*: “A new intercarrier compensation system should not only recognize existing circumstances but should also anticipate changes at least over the intermediate term, and should provide solutions that are appropriately resilient in the face of change.”

environment has three primary attributes: physical interconnection, logical (routing) interconnection, and financial arrangements.³³⁹

- Physical interconnections are made either at public exchange points, called Network Access Points (“NAPs”), or through direct private connections. While connecting at NAPs is more efficient, NAPs are frequently congested and interconnection at these locations is fraught with quality of service (“QoS”) problems. To avoid NAP congestion and to support QoS requirements, large providers often interconnect directly.
- The logical or routing aspect of interconnection refers to the IP address space available to parties of the interconnection relationship. Interconnecting entities accept each other’s traffic through either a transit or peering relationship. Transit agreements obligate one party to make available the entire Internet address space to the second party. In contrast, peering agreements only obligate the parties to provide access to their respective networks plus the networks of their transit customers.
- The financial aspect of the interconnection relationship is related to the relative amounts of traffic each entity’s customers originate and the relative size of the customer bases—essentially the value a network provider brings to the relationship. Transit arrangements are bilateral agreements that specify the amount of compensation to be paid by the transit customer and the terms of interconnection, including service guarantees. In a pure peering arrangement, one entity does not pay another compensation because exchanging traffic is deemed to be of comparable mutual benefit.

The IP market provides a “real-life” testing ground for the theory of bill and keep.

The multitude of providers initially engaged in pure peering did not compensate each other for interconnection on the commercial Internet, as they had mutual needs to interconnect with each other. As the Internet market consolidated and some entities attained market power, the compensation regime moved away from bill and keep. Large

³³⁹ National Research Council, The Internet’s Coming of Age (Washington, DC: National Academy Press, 2001) 112.

networks claimed that “free riders” with small networks dumped traffic on the backbone providers.³⁴⁰ Without compensation being exchanged, providers had an incentive to pass off traffic, like a “hot potato,” to another network at the earliest possible point to save valuable bandwidth. In response to the “free riders,” transit compensation arrangements have become increasingly common. Today most IP interconnection is based on the transit model, not the peering model. An industry that started out at bill and keep naturally evolved to compensated arrangements without regulatory intervention.

Even though the technology, end-market products and industry structures differ, the fundamental economics of interconnection for the local telephone and Internet industries are the same.³⁴¹ As the Internet industry consolidates, its structure more closely mimics that of telephony and its interconnection problems more closely align with those of telephone interconnection.

3. *Potential Market Power Abuse Is Magnified by Mergers between Tier I ISPs and RBOCs.*

Similar to the customer-provider relationship for compensation in the telephone industry, the hierarchical, bilateral model of pricing, where the smaller network pays prices set by the larger network, has become the norm in Internet pricing.³⁴² As in the local telephone market, dominant Internet providers have the ability to set prices in such a manner as to enforce their dominant position and drive competitors from the market. In addition to price discrimination, vertically-integrated firms can deny or delay access or

³⁴⁰ *Id.* at p. 116.

³⁴¹ Carolyn Gideon, “The Interconnection Pricing Problem in Local Telephone and the Internet,” Interconnecting Pricing for Competing Networks, <http://ksgwww.harvard.edu/iip/iicompol/Papers/Gideon.html>, p. 2.

³⁴² *Id.* at p. 8.

create technical incompatibilities that make interconnection more costly.³⁴³ In this manner, a vertically-integrated firm can squeeze out its rivals.

Consolidation of telecommunications companies will lead to greater market power for the leading firms, which will cause renewed concern regarding concentration in the Internet backbone.³⁴⁴ The Internet backbone market is already concentrated and will become increasingly so as the impending SBC/AT&T and Verizon/MCI mergers take place. Today, roughly a dozen ISPs provide the backbone capacity that carries the majority of the IP traffic and less than half of those are considered Tier I backbone providers.³⁴⁵ Of the Tier I providers, MCI with 27.9 percent and AT&T with 10.0 percent of the traffic have the largest market shares.³⁴⁶ In addition to being Tier I backbone providers, AT&T and MCI also provide ISP service to a significant portion of the enterprise market. Similarly, SBC and Verizon provide retail ISP service to a major portion of the residential ISP market while also providing regional backbone service. These firms not only control significant IP interconnection, but also will control significant PSTN interconnection.

Early concerns over IP backbone concentration may pale in comparison to the vertical integration effects created by these mergers. A firm with a retail end-user market

³⁴³ Jonathan Rubin, American Antitrust Institute, The Competitive Threat of the Telecommunications Mergers, p. 2.

³⁴⁴ Jonathan Sallet, The Glover Park Group, "Just How Open Must an Open Network Be for an Open Network to Be Labeled 'Open'?", February 15, 2005, http://www.firstmonday.org/issues/issues8_3/sallet/index.html

³⁴⁵ National Research Council, The Internet's Coming of Age (Washington, DC: National Academy Press, 2001) 110.

³⁴⁶ Russ Haynal's ISP Page, <http://navigators.com/isp.html> (2001).

share advantage will be in a position to price wholesale interconnection in such a way as to hamper the profitability of its retail competitors or even drive those competitors from the market.³⁴⁷ For example, if a large RBOC with a substantial base of end-user Internet access customers and significant IP backbone facilities decides to price its IP backbone service so as to squeeze its competitors out of the retail market, it would be in a position to do so.

Even with several Tier I backbone providers available, market power can be exerted because a major portion of the IP retail market is controlled by a few vertically-integrated providers. These few providers have the incentive to behave in a cartel-like manner to extract higher profits. It is naïve to believe that the mergers will result in “benevolent” competitors when these same firms, SBC and Verizon, are also petitioning the Commission for forbearance from their obligations as common carriers.³⁴⁸ Through their petitions these companies are attempting to restrict local interconnection and drive out competitors.

³⁴⁷ Carolyn Gideon, “The Interconnection Pricing Problem in Local Telephone and the Internet,” Interconnecting Pricing for Competing Networks, <http://ksgwww.harvard.edu/iip/iicompol/Papers/Gideon.html>, p. 6. “The critical issue in interconnection pricing is the possible incentive for the players with upstream market power, based on greater market share in the downstream market, to price interconnection in a way that further increases their concentration downstream, making that market less competitive.”

³⁴⁸ See *In the Matter of Petition of BellSouth Telecommunications, Inc. For Forbearance Under 47 U.S.C. §160(c) From Application of Computer Inquiry and Title II Common-Carriage Requirements*, WC Docket No. 04-405, DA 04-3507 (filed Nov. 3, 2004) and *Petition of Qwest Corporation for Forbearance Pursuant to 47 U.S.C. § 160(c) Pertaining to Qwest’s xDSL Services*, WC Docket No. 04-416, (filed Nov. 16, 2004) and *Petition of the Verizon Telephone Companies for Forbearance under 47 U.S.C. §160(c) from Title II and Computer Inquiry Rules with Respect to Their Broadband Services*, WC Docket No. 04-440, DA 04-4049 (filed Dec. 23, 2004), and *Petition of SBC Communications Inc. for Forbearance from the Application of Title II Common Carrier Regulation to IP Platform Services*, WC Docket No. 04-29, (filed Feb 5, 2004). SBC’s petition was denied by the Commission on May 5, 2005. See *In the Matter of Petition of SBC Communications Inc. for Forbearance from the Application of Title II Common Carrier Regulation to IP Platform Services*, WC Docket No. 04-29, Memorandum Order and Opinion, (rel. May 5, 2005).

The current IP interconnection situation where an ISP has sole access to their end user customers, the so-called “terminating monopoly,”³⁴⁹ as well as owning the interconnection facilities is analogous to the historical precedent of AT&T and the Bell system early in the 20th century. Even though the independents and Bell had roughly the same customer base, Bell was able to use its AT&T Long lines affiliate as leverage to drive independent operators out of the local market. Bell refused to set interconnection charges for either its local exchange or long-lines network unless the independent agreed to either sell a portion of the independent’s company to Bell or merge with the Bell company.³⁵⁰ In exchange for dropping an antitrust action against Bell, the Kingsbury commitment was signed, which halted this anti-competitive behavior.

Academics have also recognized the similarity between early telephony interconnection and IP interconnection. Joseph Bailey, Director of the Center for Electronic Markets and Enterprises at the University of Maryland Robert H. Smith School of Business, observes: “This is not very different from the pattern of development and behavior of the telegraph and telephone networks in the United States in the nineteenth century.” He concludes “regulation may then be necessary for the Internet service provision market to require companies to interconnect.”³⁵¹

There are incentives for today’s vertically-integrated companies to respond similarly to the telephone industry’s long-line/local predecessors. Yesterday’s long-line

³⁴⁹ An ISP has sole access to its Internet customer base in a similar manner as a local telephone company has sole access to its telephone customers.

³⁵⁰ Ida Walters, “Freedom for Communications,” Instead of Regulation: Alternatives to Federal Regulatory Agencies, ed. Robert W. Poole, Jr. (Massachusetts: Lexington Books, 1982) p. 117.

³⁵¹ Bailey, J. P. “The Economics of Internet Interconnection Agreements,” In McKnight, Lee W., and Bailey, eds., *Internet Economics*. Cambridge, Mass.: MIT Press.

network is replaced with today's Internet backbone in the competitive equation. In addition, the customer base will be a greater factor today because when the interconnection battles of old were being fought between Bell and the independents, the two had comparably-sized customer bases. In today's environment, small providers have far fewer customers than the merged firms. Since the size of the customer base is a significant factor in determining the "value" of the interconnection, small entities are even more negatively impacted by market concentration. These factors, coupled with the merged firms' obvious ability to use backbone interconnection as leverage in an anti-competitive manner, should warrant examination.

4. *The Commission's IP Backbone Analysis Did Not Contemplate Today's Market Concentration.*

In September of 2000 the Commission released a study of the IP backbone market which concluded that the IP backbone market should remain free of telecommunications regulation.³⁵² Since publication of the Commission's paper, the circumstances surrounding the IP backbone market have changed dramatically. The author of the Commission's paper could not have imagined the level of IP market concentration that would result from the impending merger between AT&T and SBC, as well as the merger between MCI and Verizon.

In the Commission's analysis of the IP backbone market, the study's recommendation focused on the growing trend away from uncompensated peering and toward compensated transit arrangements. The question posed in the Commission's paper was whether that trend, in and of itself, justified a regulatory policy change. The

³⁵² Michael Kende, Federal Communications Commission, Office of Plans and Policy, The Digital Handshake: Connecting Internet Backbones (Washington DC: FCC, 2000) at p. 31.

Rural Alliance does not question the imposition of transit payments; rather it believes that the focus of the analysis should now be on whether IP interconnection prices, terms and conditions are appropriate or if IP interconnection is even available at all.³⁵³

Some authors have suggested that IP industry dynamics inherently create a situation where market dominance can be abused and non-disclosure agreements will hide such abuse.³⁵⁴ Since the publication of the Commission's paper, significant IP marketplace consolidation has occurred and more is expected. Today's concerns center around interconnection availability and whether interconnection provided by companies with market power will result in either monopoly rents or prices set to seek an unfair competitive advantage in the retail Internet access market.

Michael Kende, the author of the Commission's study, observes that antitrust laws were enacted to protect consumers from market power exploitation and antitrust laws apply to all products and services, including the IP backbone. Kende points out that antitrust laws were invoked in the cases of the MCI/WorldCom and MCI/WorldCom/Sprint mergers.³⁵⁵ While antitrust laws have been used traditionally as a vehicle to prohibit mergers or break up existing entities with market power, the Rural Alliance is not suggesting that the mergers be blocked. Rather, the Rural Alliance suggests that it is appropriate to have regulatory oversight of IP interconnection,

³⁵³ Kenneth Neil Cukier, "Peering and Fearing: ISP Interconnection and Regulator Issues," at p. 6 "Interconnection and peering arrangements can in cases be discontinued with little notice on the part of the larger network.

³⁵⁴ *Id.* at p. 9.

³⁵⁵ Michael Kende, Federal Communications Commission, Office of Plans and Policy, The Digital Handshake: Connecting Internet Backbones (Washington DC: FCC, 2000) p. 24.

considering such issues as pricing, transparency³⁵⁶ and Quality of Service.³⁵⁷ Regulatory oversight would also necessarily include the elimination of non-disclosure agreements on interconnection arrangements to ensure their availability for public review. Without such intervention, Internet backbone “balkanization” will likely take place, whereby competing backbones attempt to differentiate their products by refusing to interconnect for all services.³⁵⁸

The Rural Alliance recommends that the Commission initiate a Further Notice to investigate IP interconnection issues and take the immediate step of outlawing non-disclosure agreements that shield discriminatory behaviors. Such action is not a move toward “regulating the Internet,” rather it simply assures reasonably-priced and universally-available transmission and interconnection. As concentration continues in the IP backbone and retail markets, the assumption of a competitive Internet marketplace is no longer valid.

Finally, Kende incorrectly asserts that section 230 of the Act implies that oversight of Internet interconnection should be avoided. Such reasoning is fallacious because section 230 relates to blocking of Internet content, not regulatory oversight of

³⁵⁶ Transparency refers to the Internet’s characteristic of not tampering with or restricting data flow.

³⁵⁷ Quality of Service refers to the transmission parameters associated with jitter, delay, throughput, and packet loss.

³⁵⁸ Michael Kende, Federal Communications Commission, Office of Plans and Policy, The Digital Handshake: Connecting Internet Backbones (Washington DC: FCC, 2000) p.26. “Internet backbones may thus attempt to differentiate themselves from each other by offering certain new or existing services only to their own customers. As a result, the Internet may ‘balkanize,’ with competing backbones not interconnecting to provide all services.”

interconnection.³⁵⁹ Thus, interconnection oversight does not violate section 230. Absent Commission action to investigate Internet interconnection and outlaw non-disclosure agreements, the Commission may unwittingly jeopardize the future of Internet commerce. With an open public IP network platform that is reasonably priced to all segments of the populace, the nation's economy, Internet innovation and information flow will be enhanced.³⁶⁰

5. *The Universal Service Joint Board Should Recommend a New IP High Cost Support Paradigm.*

An important issue arises from the observation that *net* future compensation will likely flow from small ISPs/LECs to large ISP backbone providers.³⁶¹ This funding flow is a reversal of the current PSTN situation where IXC's, the functional equivalent of ISP backbone providers, pay access charges to LECs, the functional equivalent of small ISPs. In the likely scenario where all voice applications migrate from the PSTN to an integrated-services IP network platform, interconnection revenues will not contribute to the support of rural broadband networks. These broadband networks will likely be the primary vehicles for reliable broadband Internet access for customers living outside of cities and towns. Inside cities there will usually be two providers: the existing broadband-enhanced telephone network and the cable television network. While

³⁵⁹ 47 U.S.C. § 230(a)(2) states that it is the United States' policy "to preserve the vibrant and competitive free market that presently exists for the Internet and other interactive computer services, unfettered by Federal or State regulation"

³⁶⁰ Cooper, Mark, "The Public Interest in Open Communications Networks," Consumer Federation of America (2004) p. 12.

³⁶¹ LECs will still charge ISPs for DSL and special access service, but the ISP backbone providers will charge small ISPs for backbone capacity. Considering that most very rural ISPs are affiliated with LECs, and as such the payments will simply circulate from one affiliate to another, the net compensation will likely flow out of rural areas toward the ISP backbone provider.

alternative technologies exist or may be developed in the future, today 99 percent of all broadband is provided either by DSL or cable modem service.³⁶²

The importance of this market structure change described above is that rural areas will be without a significant funding source to support the infrastructure. For many rural exchange carriers, intercarrier compensation represents a significant revenue component. Without such revenue, rural carriers will need to recover costs through some other means if they are to remain viable. Moreover, the expense outflows required of rural ISPs/LECs to gain IP backbone access will only exacerbate the problem. The Rural Alliance believes increases in universal service support will be necessary to support rural areas.

Current universal service policy seeks to overcome geographical location and income as factors in the penetration level for critical services. Some have suggested that the fluidity of IP applications makes the definition of a static IP universal service set difficult. In 1997, a cross-industry working team attempted to define a service performance profile as a means to define IP universal service.³⁶³ The group concluded that while service classification may be useful for consumers, the prescription of a set of IP-related universal services was, at that time, too restrictive given the industry's rapid evolution.

³⁶² “As of the end of 2003, cable providers served 16.4 million lines to residential and small-business customers, while ADSL providers served 8.9 million lines, and satellite and wireless providers served 342,000.” See *Petition of BellSouth Telecommunications, Inc. For Forbearance Under 47 U.S.C. §160(c) From Application of Computer Inquiry and Title II Common-Carriage Requirements*, WC Docket No. 04-405, DA 04-3507 (rel. Nov. 3, 2004) at p. 8

³⁶³ National Research Council, *The Internet's Coming of Age* (Washington, DC: National Academy Press, 2001) p. 214.

Among the critical policy questions needing to be addressed are as follows: How will the broadband build-out to the country's most rural areas be funded? What is the role of the universal service support system in the broadband build-out? Does IP change the set of supported services for universal service purposes? Should the supported services be defined in terms of a minimum Quality of Service level? Should universal service be directed toward infrastructure, not services?

The Rural Alliance recommends that the Commission refer the aforementioned questions to the Joint Board on Universal Service. The Joint Board should also consider the feasibility of a broadband infrastructure-based premise for high cost support, rather than a services-based premise. In addition, the Joint Board should evaluate whether universal service should be restructured to support the complementary services of both broadband and mobility because each service provides a different customer utility.

In testimony on the future of universal service, Bill Gillis, then chairman of the Rural Task Force, recommended just such an approach:

He proposed that "the FCC undertake a broad stakeholder process focused on rethinking the current Federal rules for allocating universal service dollars to support mobile wireless and the competing provision of services in rural locations."³⁶⁴

The Rural Alliance believes that successful resolution of universal service issues outlined in this section is vital to the future of rural telecommunications infrastructure.

Intercarrier compensation, while important, is but one component of the overall

³⁶⁴ Gillis, Bill, Testimony on the Future of Universal Service Hearing to the Subcommittee on Communications of the Senate Committee on Commerce, Science, and Transportation, April 2, 2003.

compensation for a telecommunications provider. Of even greater importance for rural customers and the carriers that serve them is the long-term stability of universal service.

6. *The ICF Proposal Differs Significantly from the IP Model Despite Assertions to the Contrary.*

In this Notice the Commission is considering whether economic improvements can be achieved by mandating an uncompensated regime for PSTN interconnection. The ICF has proposed a bifurcated regime that imposes bill and keep for some aspects of interconnection but not for others. Bill and keep would apply for transport and termination between the end user and a carrier's edge, a point where a carrier will receive traffic for routing within its network. On the other hand, compensation would be paid to parties providing switching and transport functions, known as Tandem Transit Service, a service which enables indirect, intraLATA interconnection between carriers.³⁶⁵

Zero compensation for transport and termination is similar to an IP peering arrangement. Nevertheless, the difference between the ICF proposal and IP peering occurs when the *interconnection value* is not equal for both parties. For IP interconnection, when the value of interconnection to the parties is different, compensation flows towards the party providing the greater value. By contrast, when traffic is unbalanced or the cost structures are asymmetrical, and thus value is differentiated between the parties, the ICF plan still confusingly calls for zero compensation.

In addition, there are other differences between IP peering and the ICF plan with respect to terminating address space. In IP peering arrangements, the entire address

³⁶⁵ See *ICF Plan* at p. 25.

space of each party is available to the other. In contrast, the ICF plan does not specify what address space is available when a carrier delivers traffic to another carrier's edge. The ICF plan simply states that "each carrier will associate relevant call routing information with the appropriate edge in each LATA."³⁶⁶ Does this mean that a carrier can choose to terminate traffic to only a portion of its network? Can a carrier choose certain NPA-NXXs for routing terminating traffic? This description seems contrary to the statement that "[e]ach carrier will establish an 'edge' or 'edges' as the point or points at which the carrier will receive traffic *for routing within its network*."³⁶⁷ The later portion of the statement seems to indicate that carriers would route traffic throughout their networks, including beyond the LATA where the traffic was delivered. Such an interpretation would be consistent with an IP peering arrangement, whereby carriers have access to each other's entire address space. Regardless of the intended meaning, the plan is unclear in this area.

Finally, the ICF appears to have modeled PSTN tandem transit after the IP transit model. In both instances the arrangements are compensated. IP transit service allows the purchaser to reach the entire IP address space. Yet under the ICF's plan for the PSTN, the buyer of Tandem Transit Service is limited to the tandem switch's LATA.³⁶⁸ This inconsistency is curious coupled with ICF's assertion that "legacy" classifications, such as interLATA and intraLATA, are no longer appropriate.³⁶⁹

³⁶⁶ *Id.* at p. 3.

³⁶⁷ *Id.* at p. 4, emphasis added.

³⁶⁸ See *ICF Plan, Appendix B* at p. 4.

³⁶⁹ See *ICF Brief* at p. 3.

The arguments favoring a bill-and-keep regime for PSTN interconnection compensation appear to fail when applied to IP interconnection arrangements. The ICF authors assert that legacy regulation associated with interconnection compensation in the PSTN space should be replaced with a bill-and-keep regime that is “sustainable and meaningful in an age of competition, rapid technological evolution, and industry-wide convergence on IP-enabled platform.”³⁷⁰ The ICF implies that bill and keep for transport and termination plus paid Tandem Transit Service is consistent with the IP compensation regime. In reality, IP interconnection agreements between ISPs are most likely compensated agreements and not pure bill-and-keep agreements. Only in the rare case of Tier I to Tier I interconnection is bill and keep still the predominant compensation arrangement. For these reasons, the ICF’s assertion that the industry must move to bill and keep for PSTN compensation as a means of addressing the market evolution to IP is not consistent with the direction of current IP compensation.

Just as the Internet evolved naturally to a compensated intercarrier framework, so too must the PSTN continue to be based on a compensated framework. Uncompensated interconnection arrangements are only reasonable when the value of interconnection to the parties is equal. Bill and keep for PSTN interconnection only makes sense when there is there is a balance of traffic and the two parties’ costs are comparable. To force bill and keep on the PSTN could only be done through regulatory fiat. It would not be a natural result based on actual experience and it is bad public policy.

³⁷⁰ *Ibid.*

VII. CONCLUSION

As is evident from the breadth and depth of these Comments, small and rural telecommunications companies and associations, as represented by the Rural Alliance, recognize the significance of this proceeding to ensuring that consumers in remote, less-populated portions of the nation have access to advanced telecommunications services in the future. While certainly the issues raised in this *FNPRM*, and hence addressed in these Comments, are complex and may even appear to be overwhelming, the Rural Alliance urges that solutions are within reach of regulators and the industry under existing Federal law.

These Comments, consistent with the comprehensive intercarrier compensation reform principles of Rural Alliance and NARUC, provide balanced, measured and rational responses and recommendations:

- Any intercarrier compensation mechanism that is adopted should promote economic efficiency, recognizing that all RSPs that use the network should pay for it. The Comments propose unification of traffic-sensitive rates for exchange access and reciprocal compensation based on embedded costs and in conformance with the Act's additional cost standard.
- Balanced cost recovery must be maintained among nationally benchmarked end-user rates, unified intercarrier compensation rates, and USF in order to preserve universal service but limit fund growth. The Comments also recommend that reductions in intercarrier revenues be offset through USF support or another mechanism, and that SLC caps should be the same for urban and rural customers to ensure rate comparability.
- Application of the Commission's interconnection rules should be clarified to ensure that network obligations unfairly benefiting other carriers should not be imposed on RLECs and that exchange access and reciprocal compensation be maintained as the law requires. The Comments also recommend that tandem access and transit services are required under a carrier's duty to interconnect, while rules governing interconnection between CMRS providers and LECs must reflect the statutory obligations of LECs, including interconnection within the LEC's network, and toll dialing parity requirements.

- Any reforms that are to be legally implemented must involve both State and Federal regulators through a constructive, collaborative process including Joint Board referrals. The Rural Alliance urges that exchange access and reciprocal compensation cannot be combined, noting that current law does not give the Commission authority over intrastate access.
- Finally, the record in this proceeding must include solutions for ISP-bound traffic as well as investigation of IP interconnection issues to ensure that the transition from the circuit-switched to the IP environment is addressed simultaneously with reforms contemplated in the circuit world. The Comments recommend that ISP traffic bound for LEC networks be subject to exchange access, and that the ESP exemption from access for ISP-bound traffic apply only to those situations where the ISP directly connects to a LEC. The Comments further recommend that IP reforms include fair interconnection standards between independent ISPs and large backbone providers, as well as a Joint Board referral for a new IP high cost support paradigm.

The Rural Alliance respectfully requests that the Commission proceed expeditiously yet judiciously in this proceeding, and carefully consider the recommendations contained in these Comments.

Respectfully submitted,

THE RURAL ALLIANCE

By: /s/Stephen G. Kraskin

Stephen G. Kraskin
Kraskin, Moorman & Cosson LLC
2120 L Street N.W. Suite 520
Washington, D. C. 20037
(202) 296-8890
skraskin@Independent-tel.com

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APPENDIX A: List of Sponsoring Companies, Consultants and Associations

Alenco Communications
Alliance Communications Cooperative, Inc.
Andrew Telephone Company
Arkansas Telephone Company
Arlington Telephone Company
Armour Independent Telephone Company
Armstrong Telephone Company
Arthur Mutual Telephone Company
Atlas Telephone Company
Ayrshire Farms Mutual Telephone Company
Beehive Telephone Company
Beresford Municipal Telephone Company
Big Bend Telephone Company
Blair Telephone Company
Blue Valley Tele-Communications
Brazos Telephone Cooperative, Inc.
Brenton Woods Telephone Company
Bridgewater-Canistota Independent Telephone Co.
Cambridge Telephone Company
Cameron Communications
Canadian Valley Telephone Company
Canby Telephone Association
Cap Rock Telephone Cooperative, Inc.
Carnegie Telephone Company
Central Oklahoma Telephone Company
Central Texas Telephone Cooperative, Inc.
Cherokee Telephone Company
Cheyenne River Sioux Tribe Telephone Authority
Chickasaw Telephone Company
Chippewa Telephone Company
CHR Solutions, Inc.
Cimarron Telephone Company
Citizens Telephone Corporation (Indiana)
City of Brookings Utilities
City of Faith Telephone Company
Clarks Telecommunications Company
Coleman County Telephone Cooperative, Inc.

Colorado Valley Telephone Cooperative, Inc.
Comanche County Telephone Company, Inc.
Community Telephone Company, Inc.
Consolidated Communications
Consolidated Telco, Inc.
Consolidated Telecom, Inc.
Consolidated Telephone Company
Cooperative Telephone Company
Council Grove Telephone Company
Craigville Telephone Company
Craw-Kan Telephone Cooperative
Cross Telephone Company
Cumby Telephone Cooperative, Inc.
Cunningham Telephone Company
Daviess-Martin County Rural Telephone
Dell Telephone Cooperative, Inc.
Dixville Notch Telephone Company
Dobson Telephone Company
Doylestown Telephone Company
Dumont Telephone Company
Dunbarton Telephone Company
Eastern Nebraska Telephone Company
Eastex Telephone Cooperative, Inc.
Egyptian Telephone Company
Enhanced Telecommunications Corporation
ENMR Telephone Cooperative, Inc.
Etex Telephone Cooperative, Inc.
FairPoint Communications, Inc.¹
Farmers Cooperative Telephone Company
Farmers Mutual Coop Telephone Company
Fenton Cooperative Telephone Company
Five Area Telephone Cooperative, Inc.
Flat Rock Tel. Coop
Franklin Telephone Company
Fred Williamson and Associates, Inc
Ganado Telephone Company, Inc.
Genesco Telephone Company
Germantown Independent Telephone Company
Glandord Telephone Company

¹ FairPoint Communications is a holding company with 27 local telephone companies.

Golden Belt Telephone Association
Golden West Telecommunications Coop
Goldfield Telephone Company
Granite State Telephone Company
Great Plains Communications, Inc.
H&B Communications, Inc.
Hancock Rural Telephone Company
Hartington Telecommunications Company
Haviland Telephone Company
Heart of Iowa Communications Cooperative
Hershey Cooperative Telephone Company
Hiawatha Telephone Company
Hinton Telephone Company
Hubbard Coop Telephone Association
Humboldt Telephone Company
Huxley Communications Cooperative
Indiana Exchange Carrier Association
Industry Telephone Company
Interstate Communications
Interstate Telecommunications Coop
James Valley Cooperative Telephone Company
JBN Telephone Company
Jefferson Telephone Company
K&M Telephone Company
Kadoka Telephone Company
KanOkla Telephone Association
Kennebec Telephone Company
La Ward Telephone Exchange, Inc.
LaHarpe Telephone Company
Lake Livingston Telephone Company
Laurel Highland Telephone Company
Lennon Telephone Company
Liberty Communications
Lipan Telephone Company, Inc.
Livingston Telephone Company
Lone Rock Coop Telephone Company
Lost Nation - Elwood Telephone Company
Madison Telephone
Marne & Elk Horn Telephone Company
Matanuska Telephone Association Cooperative
McCook Cooperative Telephone Co.

McLean & Brown, Inc.
Medicine Park Telephone Company
Middle Point Home Telephone Company
Middleburgh Telephone Company
Mid-Plains Rural Telephone Cooperative, Inc.
Midstate Communications, Inc.
Midway Telephone Company
Missouri Valley Communications, Inc.
Modern Coop Telephone Company
Moultrie Independent Telephone Company
Moundridge Telephone Company, Inc.
Mt Rushmore Telephone Company
Mutual Telephone Company (Iowa)
Mutual Telephone Company (Kansas)
Nebraska Central Telephone Company
Nemont Telephone Cooperative, Inc.
New Hampshire Telephone Association
New Lisbon Telephone Company, Inc.
Nortex Communications - Telephone Operations
North Pittsburgh Telephone Company
Northeast Nebraska Telephone Company
North-Eastern Pennsylvania Telephone Company
Northern Arkansas Telephone Company
Northwest Telephone Coop
Oklahoma Rural Telephone Coalition
Oklahoma Western Telephone Company
Ontonagan County Telephone Company
Oregon Farmers Mutual Telephone Company
Organization for the Promotion and Advancement of Small Telephone Companies
Ottoville Mutual Telephone Company
Panhandle Telephone Cooperative, Inc.
Partner Communications Coop
Peoples Telecommunications
Peoples Telephone Cooperative, Inc.
Pine Telephone Company, Inc.
Pioneer Communications
Pioneer Telephone Association, Inc. .
Pioneer Telephone Cooperative, Inc.
Plains Cooperative Telephone Association
Poka Lambro Telephone Cooperative, Inc.
Pottawatomie Telephone Company

Prairie Grove Telephone Company
PrairieWave Community Telephone, Inc.
Project Telephone Company
Rainbow Telephone Co-op
Randolph Telephone Company
RC Communications, Inc.
Ringsted Telephone Company
Riviera Telephone Company, Inc.
Roberts County Telephone Cooperative Assn.
Rochester Telephone Company, Inc. (Indiana)
Rock County Telephone Company
Rural Telephone Service Company
Rye Telephone Company
S & A Telephone Company
S & T Telephone Coop.
Salina-Spavinaw Telephone Company
Sandwich Isles Communications, Inc.
Santa Rosa Telephone Cooperative, Inc.
Santel Communications Cooperative
Shidler Telephone Company
Sioux Valley Telephone Company
Siskiyou Telephone Company
South Central Telephone Association (Oklahoma)
South Central Telephone Associaton (Kansas)
South Dakota Telecommunications Association
South Park Telephone Company
South Plains Telephone Cooperative, Inc.
Southern Kansas Telephone Company
Southwest Oklahoma Telephone Company
SpencerMunicipal Utilities
Stanton Telephone Company
Star Telephone Company
State Independent Telephone Association (Kansas)
Stockholm-Strandburg Telephone Company
Stratford Mutual Telephone Company
Sully Telephone Association
Swayzee Telephone Company
Swisher Telephone Company
Sycamore Telephone Company
Taylor Telephone Cooperative, Inc.
TCA, Inc.

TDS Telecom²
TelAlaska
TELEC Consulting Resources
Telephone Service Company
Terral Telephone Company
Texas Statewide Telephone Cooperative
Three River Telco
Toledo Telephone Company, Inc.
Topsham Telephone Company
Totah Communications, Inc.
Tri-County Telecom, Inc.
Twin Valley Telephone, Inc.
Union Telephone Company
United Telephone Association
Valley Telecommunications Coop.
Valliant Telephone Company
Venture Communications Cooperative
Vermont Telephone Company
Vivian Telephone Company
Volcano Telephone Company
Waitsfield and Champlain Valley Telecom
Warinner, Gesinger & Associates, LLC
West River Cooperative Telephone Company (Bison, SD)
West River Telecommunications Coop. (Hazen, ND)
West Texas Rural Telephone Coop., Inc.
Western New Mexico Telephone Company, Inc.
Western Telecommunications Alliance
Western Telephone Company
Wes-Tex Telephone Cooperative, Inc.
Wheat State Telephone
XIT Rural Telephone Cooperative, Inc.

² TDS Telecom is a holding company with 111 local telephone companies.

APPENDIX B: The Economic Cost of Mandatory Bill and Keep

Dale Lehman¹

The Staff report attached to the *FNPRM* (Appendix C) discusses efficiency properties of bill and keep and addresses previous comments raised about bill and keep as an interconnection regime. This paper reexamines the Staff report by carefully defining economic efficiency, and then analyzing the costs and benefits of bill and keep relative to a unified (but nonzero) interconnection price. Since a number of proposals endorse some version of bill and keep, it is important to understand the implications of *mandating* bill and keep interconnection. While voluntary negotiation of bill and keep can be expected to generate net economic benefits, such optimism should not accompany a mandatory bill and keep regime.

1. Economic Efficiency

Efficiency has several dimensions including: productive efficiency, internalization of call externalities, maximization of mutually profitable trades, administrative efficiency, and dynamic efficiency (efficient investment incentives). Bill and keep should be evaluated with respect to these (potentially conflicting) dimensions. The tension between efficient interconnection pricing and universal service must also be recognized.

Productive Efficiency:

¹ Dale Lehman is Director of the MBA Program in Telecommunications Management at Alaska Pacific University. He has taught at a dozen universities and has held positions at Bellcore and SBC. His publication and consulting experience is mostly in the telecommunications and information industries, where he has focused on market structure, new services, and public policy.

Productive, or technical, efficiency is the principle that goods and services are produced at minimum cost. One of the purported advantages of bill and keep is that it provides incentives for the terminating carrier to minimize its termination costs while the current access charge system does not. There are two caveats that should accompany this purported advantage. First, while the current access charge regime does not provide cost reduction incentives in itself, there are other competitive pressures on LECs that may serve this purpose. In particular, the competitive threats from mobile services (and increasingly, VoIP services) mean that higher-than-necessary termination costs are penalized by the marketplace. Second, bill and keep provides incentives for service providers to overuse the facilities of the terminating carrier. This could apply to both transit and switching. Since termination is being provided for a zero price, other carriers will not be concerned with minimizing these costs. This has been a concern for Internet backbone providers where peering arrangements (bill and keep) provide incentives for carriers to dump traffic off at the earliest possible interconnection point. It will remain a problem for bill and keep schemes where originating LECs are responsible for delivering traffic to IXC POPs. Bill and keep removes incentives to include these transit and termination costs when relocating POPs. Absent any payment to the originating or terminating LEC, these incentives will be to overuse the transport facilities of LECs since they are not the financial responsibility of the IXC.

Internalization of Call Externalities:

When individual decisions convey benefits or costs on others (that don't make the decisions), externalities may be present. Economic efficiency dictates that decisions reflect the full costs and benefits, including those that fall on other parties than the

decision maker. The Staff report discusses in some detail the shared nature of benefits from telephone calls. While it is generally true that call benefits are shared by the caller and the called party, this is mostly irrelevant to the selection of an efficient interconnection price. Some calls entail only benefits to the caller, perhaps even with costs imposed on the called party (e.g., telemarketing calls). Other calls primarily provide benefits to the called party (e.g., 800 service). On average, it is unlikely that the benefits are shared equally since the caller can initiate a call with no consultation or agreement by the called party. Bill and keep appears to make the most sense if the benefits of a call are shared equally between the originator and recipient of a call (and if the cost structures of the originating and terminating carriers are similar).²

In any case, interconnection pricing is not about allocating the benefits of a call – it is about recovering the costs associated with call origination and termination. If the termination costs are not zero, then the termination price should not be zero. Similarly, if the call origination costs are not zero neither should the origination price. Yet, the Staff report defines bill and keep as the absence of any payment to a carrier for the origination or termination of a call. While no interconnection regime is likely to fully account for externalities, bill and keep removes an instrument, access charges, that can be used to reduce such externalities.³

Maximization of Mutually Profitable Trades:

² The call externality issues associated with B&K were debated in two articles in March 2002 issue of *The Review of Network Economics*: J. Wright, “Bill and Keep as the Efficient Interconnection Regime?” and P. DeGraba, “Bill and Keep as the Efficient Interconnection Regime? A Reply,” Volume 1, Issue 1.

³ Call externality issues are mitigated somewhat by the fact that much of the traffic is reciprocal in nature. For parties that call each other often, the externalities are probably internalized.

Economic efficiency dictates that consumers purchase as long as marginal benefits exceed marginal costs but not when marginal costs exceed marginal benefits. When bill and keep is voluntarily negotiated between carriers, it will generally promote efficiency since the exchange is mutually profitable. In markets, if prices do not reflect costs accurately, consumption will generally be either excessive or deficient. Indeed, one of the principle inefficiencies of current access charges is that they send inefficient price signals to consumers: interLATA and intraLATA toll calls are priced too high relative to their incremental costs, thereby causing too little use. To the extent that different technologies face different access charges (due to regulatory regimes), then consumer choices between these technologies will be skewed. So, bill and keep offers the advantage of erasing such differences, but so would any unified intercarrier compensation regime. However, bill and keep is a unified regime with a price of zero that may create its own inefficiencies.

Bill and keep will not provide efficient outcomes when traffic and/or costs are imbalanced. Since a goal of ICC reform is to have a unified system, application of bill and keep to all ICC arrangements is likely to be inefficient for some, if not all, of these. The myriad types of networks and technologies used to complete calls only compounds the potential inefficiencies of bill and keep. Evidence from other industries supports this view. Internet backbone arrangements generally take the form of either *peering* (essentially a bill and keep arrangement) or *transiting* (essentially an access charge arrangement). Peering is generally adopted only when network traffic and costs are relatively balanced. In particular, when small networks connect to large backbone providers, peering is not used. In credit card networks, there is an *interchange fee* that

flows from the acquiring bank (the merchant's bank) to the issuer (the cardholder's bank). This fee is not zero – it reflects the costs to the issuer of attracting and retaining the cardholder.⁴ So, markets generally recognize unbalanced traffic and/or costs by not adopting bill and keep.

Administrative Efficiency:

Regulatory goals should be achieved at minimum administrative cost. This is one of the major appeals of bill and keep, since metering and billing of intercarrier traffic becomes unnecessary. While the simplicity of bill and keep is apparent, these efficiency gains are likely to be overstated. Bill and keep replaces the known monitoring and billing problems associated with access charges⁵ with the relatively unknown tasks associated with interconnection points. Definition of interconnection points is critical to bill and keep and traffic will still need to be monitored in order to ensure that the interconnection points are chosen correctly. It may be harder to move interconnection points than to change the level of access charges since facility investments are likely to be sunk once the points are defined. As technologies evolve, the meaning of interconnection points may change. For example, mesh wireless networks may not easily fit with definition of some interconnection points. So, bill and keep's apparent administrative efficiency, in part, results from the fact that we have limited experience with defining interconnection

⁴ In fact, it is generally argued that the correct interchange fee should not even be cost-based. This is so that the network externalities associated with attracting cardholders can be internalized. See "An Economic Analysis of the Determination of Interchange Fees in Payment Card Systems," J. Rochet and J. Tirole, *The Review of Network Economics*, Vol. 2, No. 2, June 2003.

⁵ It is worth noting that many of the current administrative problems derive from the lack of a unified ICC scheme rather than from the existence of access charges, per se. When regulatory arbitrage opportunities are removed via a unified charge, only the costs of measurement and billing will remain, but not the need to monitor whether traffic is being "disguised" or routed improperly.

points. Since the financial responsibility of carriers is defined at these interconnection points, there will be incentives to overuse other carriers' facilities once the points are defined. Such incentives are largely mitigated by the presence of access charges.

Dynamic Efficiency:

Dynamic efficiency refers to ensuring that incentives are adequate for future investment, but not excessive. It should be noted that there is frequently a tension between dynamic and static economic efficiencies.⁶ Bill and keep does not contribute to dynamic efficiency since it undermines the incentive and ability of terminating (and possibly originating) carriers to invest in new capacity and capabilities. Bill and keep imposes the responsibility for costs squarely on a carrier's subscribers. Whatever the economic virtues of such an arrangement, it jeopardizes investment in rural areas. The whole rationale for universal service policies is that consumers in high cost areas should have comparable services at comparable rates. Given that costs are higher in these areas, asking consumers to bear their higher costs is directly contrary to universal service policy – whatever its justification may be in terms of economic efficiency. Put another way, universal service policy may be good public policy but may not be economically efficient. Given that it *is* policy, dynamic efficiency requires adequate investment incentives for rural carriers that serve high cost areas – adequate to provide comparable services at comparable rates, including advanced services. Bill and keep, by removing a significant portion of the revenue stream and re-imposing that on high cost customers, does not fulfill this obligation.

⁶ A common example is patents: a patent-holder is given temporary monopoly power, and the right to charge prices well above marginal cost, in exchange for enhancing the incentive to invent and innovate. In essence, some static economic efficiency is foregone in order to promote dynamic efficiency.

Summary:

Seen in the light of economic efficiency, bill and keep is one particular compensation scheme in which there is a unified compensation rate of zero. The apparent efficiency of *voluntary* bill and keep does not apply to *mandatory* bill and keep arrangements. B&K will not generally be efficient except in special circumstances (relatively balanced traffic and cost structures). The best evidence of this is the fact that other industries where inter-firm compensation takes place in an unregulated setting do not generally use bill and keep (Internet backbone services, wireless roaming, financial interchange fees). Bill and keep may serve to promote administrative efficiency, but at the risk of jeopardizing many of the other efficiency measures. Even the administrative efficiency of bill and keep is overstated, due to the fact that it resolves many of today's known administrative problems while creating new problems that we don't yet fully understand (issues associated with defining and monitoring interconnection points).

2. *Competitive Neutrality*

The focus on competitive issues in the Appendix is misplaced. The Appendix is concerned with incumbents receiving payment from competitors rather than customers – but interconnection rates are a form of payment from wholesale customers. The fact that some of these wholesale customers may, at the margin, be competitors does not alter the basic fact that interconnection is generally a complementary, not a competitive, service.

Issues of competitive and technological neutrality call for a unified ICC scheme – at least a reduction in the arbitrage opportunities present in current ICC schemes. Bill and keep is a unified scheme – but at a zero price. Any unified scheme will promote

neutrality among different ways of delivering services. Bill and keep is not neutral with respect to market structure, however.

Bill and keep appears to work best for large vertically integrated providers. Rural LECs become vulnerable under bill and keep. Depending on the version of bill and keep, they may be responsible for delivering traffic either to the terminating LEC, to the IXC POP, or to their network edge. In all these cases, they will be reliant on other carriers to carry their traffic for calls that leave their service areas. The issue is what sort of bargaining power will they have negotiating agreements with these transiting carriers? The implicit assumption in bill and keep is that there is a competitive market for transit services – however, the wholesale market available to rural LECs may not be very competitive and may become less competitive in the face of the consolidation in the industry. One example concerns the use of tandem switches to deliver traffic outside of a rural LEC’s service area. These tandem switches are generally owned by either RBOCs or large independents and bill and keep would preserve payment for the use of these tandem switches. Yet it would appear that a small rural LEC would have little alternative to the use of the tandem switch in its region. The market power possessed by the owner of this tandem switch appears to be at least as great as the market power possessed by a terminating LEC.⁷

It is also unclear how many IXCs will remain available to the originating LEC and its customers. Bill and keep makes more sense when the originating carrier is the

⁷ This is the so-called “terminating access monopoly” that is the cause of much concern in the Staff report. I would point out that (1) it only applies to terminating LECs whose access charges are not regulated, and (2) the terminating LECs market power is increasingly offset by the myriad choices that consumers have for receiving calls (wireless, PSTN, Internet, etc.). On the other hand, market power possessed by tandem switch and/or transit providers is not even addressed in the Staff report.

originating LEC and it is responsible for delivering traffic to the terminating LEC. Rural LECs will generally require another carrier to provide either retail or wholesale long-haul transport. Consolidation in the industry makes it unclear how competitive these services will be for rural consumers and bill and keep will only exacerbate this uncertainty. As the industry moves towards vertically integrated providers, rural LECs and their customers will increasingly rely on a small number of vertically integrated providers to transit their traffic. It may even be the case that these vertically integrated providers will be competing with the rural LEC for some of its customers. The potential for transiting carriers to have market power over rural LECs should not be underestimated. Bill and keep places the rural LEC in a vulnerable, and potentially unstable, position.

3. Cost Causation

A more unified system of interconnection payments is required if regulatory arbitrage and instability are to be addressed. The issue, then, is whether the unified price should be zero or a positive price. Bill and keep arrangements are available to other industries with similar features to telecommunications (“two-way networks”), including Internet traffic, wireless communications, and credit card services. None of these industries has adopted a uniform policy of bill and keep. Bill and keep arrangements are voluntarily negotiated where the parties believe it is in their interests to do so. Forcing bill and keep on the telecommunications industry will lead to inefficiencies wherever parties would not voluntarily negotiate a bill and keep arrangement.

If the price for origination and/or termination of traffic is to be positive, how should it be set? The NPRM raises a number of questions regarding cost causation and the measurement of costs. These are difficult issues, as there are choices among

embedded cost, forward-looking cost, average cost, marginal cost, incremental cost, long-run cost, and short-run cost. Beyond the appropriate measurement of cost, there are issues regarding the proper way to structure prices to recover costs. Rather than attempt a comprehensive review of cost concepts, I offer a few observations to clarify some of these issues.

It may be helpful to think of the extreme case of a rural carrier with a single switch. All interoffice transport costs and some switching costs are caused by the origination and termination of traffic that involves other carriers. Of course a network constructed only to serve the local community would have less value than a network built to allow interconnection to other areas. It is not meaningful to ask whether the increased value of the interconnected network offsets the costs of interconnection – if it is a high cost area, the consumers are generally not even paying the full costs of their connections to the stand-alone local network. It is not clear whether interconnection prices should only recover the costs associated with interconnection.⁸ If public policy is to support the costs of local facilities and network interconnection in high cost areas, this support must come from somewhere other than the high cost subscribers themselves.

In any case, the Commission seeks to determine what costs are caused by interconnection. The Staff report suggests that little or no costs are caused by the termination of traffic. A number of observations are in order:

- The answer to this question will differ across different types of companies, since companies will differ in the extent of the interoffice network they build

⁸ I acknowledge that there are legal questions concerning what interconnection prices can and cannot recover. Rather than offer an opinion on this, I merely am pointing out that the public policy question of how support should be provided has no obvious answer.

for their own internal requirements. Thus, the facilities that are incremental to interconnection services will differ across companies.

- To the extent that a company would have an extensive interoffice network even without interconnection, the incremental costs associated with interconnection will be smaller. This observation applies to transit networks as well as local networks. What is the incremental cost of providing tandem switching and transit services by an RBOC to a rural LEC? The RBOC generally builds these facilities for its own needs and the incremental traffic of the rural LEC is a relatively small increment. Yet, bill and keep proponents ask that tandem switching and interoffice transport be compensated but not local origination or termination. It is not clear that the cost-causation principles are any different in these contexts.
- Additional peak load traffic clearly causes switching and transport facilities to be added. The more difficult question is whether minutes of use (“MOU”) is the best measure of cost-causation or whether a different measure (such as capacity, peak-period usage, etc.) is more appropriate. While a general answer to this question is difficult, it is not material to the choice between bill and keep and a unified positive price interconnection regime. If there is a belief that there is a weak link between MOU and network costs, that belief should not be used to justify charging a zero price, rather, a positive interconnection price should be established based on a more appropriate cost-driver than MOU.

- Finding a better measure of traffic (than MOU) that causes costs may be difficult. The appropriate measure may differ between voice and data networks, so finding a single best measure may not be possible. Many of the problems with current access charges can be reduced through a more unified interconnection price regime and continued efforts to make all universal support explicit. Bill and keep is a draconian “solution” that may lead to many new problems.
- The view that network costs are unrelated to MOU may be overstated. VoIP traffic appears to be like any other data, and MOU is generally not a good measure of cost-causation for data traffic. Future VoIP services, however, are likely to be differentiated by *quality*. Quality will require prioritization of packets and it is unclear how to best measure cost-causation for prioritized services. It is unlikely that bandwidth or connections alone will serve as the basis for pricing differential service quality.

Another issue concerns whether termination costs should be measured on an average, an incremental, or a marginal basis. While economic theory generally supports pricing at marginal cost, there are practical limitations to measuring marginal costs, and there is an exception where average costs are above marginal costs as would appear to be the case with call origination and termination in rural areas. Many of the switching and transport facilities are lumpy investments and the scale of traffic in rural areas is low relative to the capacity of these facilities. As a result, the average cost is likely to be considerably higher than the marginal cost. Pricing at marginal cost is efficient from the static point of view of maximizing the mutually profitable trades but it fails at dynamic

efficiency since it would force the carrier to operate at a loss. It is not an option to recover this deficiency from its customers since they already do not pay the full cost of their local loop facilities.

Economic efficiency generally calls for the difference between average and marginal costs to be recovered from the most inelastic customers. It is possible that this might entail raising monthly charges for high cost subscribers (provided that they don't exceed what is affordable). In fact, some proposals to deaverage SLCs appear to shift the high cost recovery burden to those that live in high cost areas. This may or may not be efficient, depending on the relative elasticities of demand of high and low cost subscribers. But, to the extent it is efficient, it clearly conflicts with the principles articulated in section 254 of the Act. Section 254 calls for "comparable services at comparable rates" and not for efficient pricing that might deviate significantly from this. This is a tension between economic efficiency and universal service that must be recognized in regulatory policy.

Difficulties in recovering the excess of average over marginal costs are compounded by limitations on the avenues rural carriers have to recover costs from their subscribers. To the extent that the costs are usage sensitive and bill and keep requires the rural carrier to bear these costs, they often cannot recover these costs through efficient usage-based charges to their subscribers. Many States have statutory bans on the use of local measured service. Raising the fixed monthly charge to recover these costs runs directly into the conflict between efficiency and universal service principles.

The NPRM also raises questions of whether costs should be forward-looking or embedded. Forward-looking cost measures, such as TELRIC, are well grounded in

economic theory. Accurate measurement of such costs has proven elusive, however, and the difficulties are particularly severe for small rural LECs. There is no chance for errors in measurement to average out across a large number of exchanges so the forward-looking cost measurement would need to be accurate at the exchange level. Current forward-looking cost models do not meet this level of accuracy. Further, it is necessary to validate any forward-looking cost measure. Embedded cost is the only available practical way to determine whether forward-looking cost estimates are reasonable. I have written on this subject before, and I believe the conclusion is still the same: embedded cost is the only reasonable way to measure costs for the rural ILECs.⁹

4. Market Structure Issues

Bill and keep implicitly assumes today's market structure. This can be seen in the original bill and keep proposal,¹⁰ where rural LECs would be responsible for delivering traffic to the IXC POP, or the ICF proposal for rural LECs to deliver traffic to their network edge. This presumes the existence of a competitive IXC market to carry the call to the terminating LEC. Several structural features in this arrangement are uncertain. Stand-alone IXCs are rapidly disappearing. Vertically integrated providers are decreasing in number. The availability of a transiting carrier to pick up traffic at competitive rates is an open question in the future. None of the bill and keep proposals indicate who would be responsible to deliver such traffic to the terminating carrier, nor do they indicate how the terms would be negotiated.

⁹ See, for example, D. Lehman, "Universal Service and the Myth of the Level Playing Field," NTCA/OPASTCO White Paper, August 2003.

¹⁰ Patrick DeGraba, "Bill and Keep at the Central Office As the Efficient Interconnection Regime," OPP Working Paper Series No. 33, Federal Communications Commission, December 2000 ("*COBAK Paper*").

Further complications arise if the vertically integrated carriers are also wireless competitors to the rural LECs. It is not hard to imagine that such a carrier might refuse to accept interexchange traffic from the rural LEC on competitive terms when it could provide end –to-end wireless service as an alternative (to some, but probably not all, of the rural customers). Change is inevitable in this industry and tomorrow’s market structures may not resemble today’s. Bill and keep poses particular dangers to rural consumers as market structures evolve. Rural consumers are often not served by the vertically integrated carriers for whom bill and keep may make sense. Regulatory policy should not *dictate* a market structure, yet bill and keep places the stand-alone rural LEC in a highly uncertain state. Uncertainty reduces the access to capital and undermines the ability and incentive to invest in rural facilities.

5. Summary

Bill and keep appears to offer a “quick fix” to many of today’s administrative problems associated with intercarrier compensation. As carriers become increasingly vertically integrated and the industry consolidates, bill and keep gains attractiveness to the major carriers. When bill and keep is analyzed more deeply, however, its benefits become tarnished. It is not generally an efficient interconnection regime for carriers that do not voluntarily adopt it. It fails to recognize cost and traffic imbalances and it fails to specify efficient recovery of high network costs in rural areas in ways that are consistent with universal service principles.

Bill and keep also exacerbates uncertainty. Responsibilities for future delivery of rural traffic, and assurances that the terms for arranging such delivery will be competitive, are unclear. The apparent administrative simplicity of bill and keep must be

weighed against these unknowns. The importance of dynamic efficiency and investment in rural infrastructure must be acknowledged. Bill and keep simply places the burden of high network costs in rural areas on the rural customers themselves.¹¹

The NPRM raises some difficult issues regarding cost causation and measurement. Costs associated with the origination, transport, and termination of rural traffic appear to be similar in nature to the costs of tandem switching and transport between switches in the interexchange network. Bill and keep singles out the rural costs for a zero price while preserving the interexchange network costs for market-based pricing (and fails to address the future competitiveness of the market that would set such prices). Again, the result is increased uncertainty for rural carriers and reduced incentives for rural investment.

Most of the serious distortions in current access charges can be reduced or eliminated through a *cost-based and unified* access charge regime. It is not necessary to impose on rural areas the uncertainties associated with bill and keep. The administrative simplicity of bill and keep is an illusion – it simply shifts the presently unknown burdens to the future. The best evidence that mandatory bill and keep is not an efficient interconnection regime is that it has not been adopted by any industry. Internet backbone traffic, wireless roaming, and credit card networks all permit bill and keep but do not adopt it as a mandatory policy. This should caution policymakers that it is not the panacea that its proponents present.

¹¹ *Id.* at footnote 55. “As previously noted, there is a slight exception to the general rule that the parties should equally split the cost of a call. Specifically, if one network has higher costs than another because it offers more features, such as mobility, it appears reasonable to require the customer subscribing to, and benefiting from, the more expensive network to pay the higher costs.” Application of this logic to higher network costs resulting from low population densities flies in the face of section 254 of the Act.